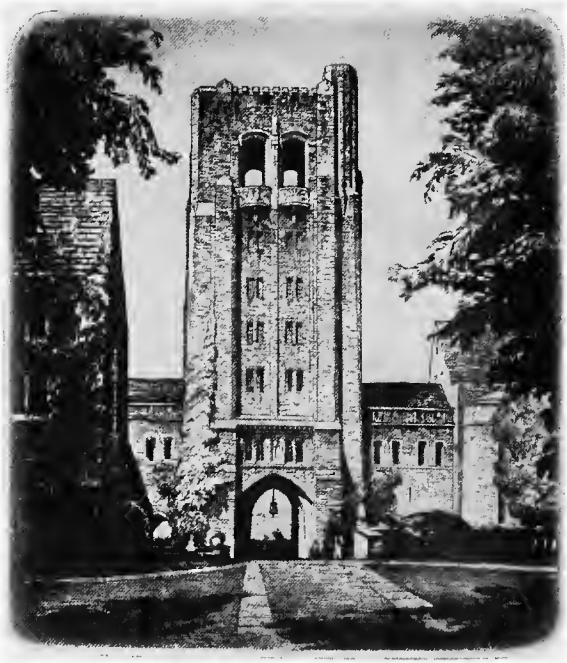

THE

PRINCIPLES OF THE LAW

RELATING TO

CORPORATE LIABILITY FOR ACTS OF PROMOTERS.

BEING THE SHARSWOOD PRIZE THESIS IN THE LAW DEPARTMENT OF THE UNIVERSITY OF PENNSYLVANIA FOR THE YEAR EIGHTEEN HUNDRED AND NINETY-SEVEN.

BY

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IS LARGELY INDEBTED, THIS TREATISE IS

DEDICATED.

PREFACE.

As the title indicates, the following pages are concerned primarily with a consideration of the liabilities to which a corporation may be subjected by its promoters.

Preparatory to a discussion of the main subject, however, it seemed necessary to review briefly the character, position and liabilities of the promoters themselves.

Part I. deals with this portion of the subject.

Part II. treats of the several theories upon which the courts have based the corporate liability, and the object has been to reproduce so far as possible the law as it is to be found in the cases.

Part III. has been devoted to a consideration of the underlying principles upon which the decisions rest.

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THE

PRINCIPLES OF THE LAW

RELATING TO

CORPORATE LIABILITY FOR ACTS OF PROMOTERS.

PART I.

PROMOTERS: THEIR RELATIONSHIPS AND LIABILITIES.

CHAPTER I.

§ 1. *Who are promoters?*

It may be said, generally, that any person who does an act with reference to the formation of a company or in aid of its organization is, as regards that act, a "promoter" of the company. As the term originated in trade and not in the law no technical legal definition is possible, but it has been well described in the following manner: "In the law relating to corporations, those persons are called 'promoters' of a company who first associate themselves together for the purpose of organizing the company, issuing its prospectus, procuring subscriptions to the stock, securing a charter, etc."[1] Or as was said by Bowen, J.,[2] it is a term, "usefully summing up in a single word a number of business operations familiar to the commercial world, by which a company is generally brought into existence."

[1] Black's Law Dictionary.

[2] Whaley Bridge Calico Printing Co. *v.* Green, L. R. 28, Q. B. D. 351.

The only requisite, therefore, to bring one within the meaning of the term is, that he shall have performed some act with a view to the formation of a company. As to what acts are usually done in the projection or floating of a corporation, is more a matter of business experience than of law, but among the most usual and necessary might be mentioned (those to which reference has already been made), viz., the issuing of the prospectus, inducing others to subscribe for stock, and obtaining the charter.

§ 2. *Relationship between corporations and their promoters.*

Now, although any act done with reference to the creation of a company will constitute one a promoter, it does not follow that a status is created. The relationship thereby established has no significance except as regards the act done. That is to say: with respect to that act, the one doing it is a promoter and subject to all the rights and liabilities which that term implies; but if he should subsequently abandon the enterprise he could not be held for acts done after his connection with the project had ceased, on the broad ground that he was a promoter of the company.

What rights and liabilities, then, does this term imply? Promoters are universally held to be corporate fiduciaries, standing in a relation of trust and confidence towards the projected company and the stockholders, and bound to exercise *uberrimam fidem* towards both.[1] This arises from the fact that promoters usually hold themselves out as deeply interested in the proposed corporation, and as acting for it. They take upon themselves to bring into existence this creature of the law which, in its inchoate state, is completely at their mercy, unprotected by impartial agents acting solely for the benefit of the stockholders. In view of these circumstances, the acts of the promoters are strictly scrutinized.[2] Since they

[1] Densmore Oil Co. *v.* Densmore, 64 Pa. 43 (1870); Chandler *v.* Bacon, 30 Fed. 538 (1887); Emma Silver Mining Co. *v.* Grant, L. R. 11 Ch. Div. 918 (1878); Simons *v.* Vulcan Oil & Mining Co., 61 Pa. 202 (1869); McElhenny's App., 61 Pa. 188 (1869); Bagnell *v.* Carlton, L. R. 6 Ch. Div. 376 (1877).

[2] Sombrero Phosphate Co. *v.* Erlanger, L. R. 3 App. Cas. 1218.

stand in a trust relation, they are prohibited from making any profit other than is common to all the stockholders, or receiving any secret advantage whatsoever, and this relation exists even in favor of those who subsequently become stockholders.[1]

The results of the cases on this question may be summed up in four propositions:

(1.) Where a promoter buys property intending to sell it to the company (already in process of formation) he cannot make a profit on the transaction without the fullest disclosure.[2]

(2.) But where one owns property he is at liberty to form a company and sell to it at any price and without disclosing his profit: provided, only, however, that he make no fraudulent misrepresentations.[3]

(3.) Where one buys property and soon after begins to promote a company, and declares that he bought the property for the company, and effects a sale to the company, he is liable for any profit made, on the ground that he has alleged that he acted as an agent in the matter, and may not now be heard to claim that he acted only for himself.[4]

(4.) If a promoter receive a gift or commission from the vendors of property for arranging a sale to the company, he must account therefor (less the amount of his disbursements); for he may not secretly derive any benefit over the other members in any transaction to which the intended company is a party.[5]

It results also from this trust relation that if the project fails, the promoters are bound to return the subscriptions to the stockholders, and failure to do so renders them liable as for a misuse of trust funds.[6]

It is evident from these results that this relation is of a fiducial character and is similar to that existing between trustee and *cestui que trust*, principal and agent, or partner and

[1] Densmore Oil Co. *v.* Densmore, 64 Pa. 43 (1870).
[2] Emma Silver Mining Co. *v.* Grant, L. R. 11 Ch. Div. 918 (1878).
[3] Densmore Oil Co. *v.* Densmore, 64 Pa. 43 (1870).
[4] Simons *v.* Vulcan Oil Co., 61 Pa. 202 (1869).
[5] Emma Silver Mining Co. *v.* Grant, L. R. 11 Ch. Div. 918 (1878).
[6] Nockles *v.* Crosby, 3 B. & C. 814.

partner. In fact, in *Bagnell* v. *Carlton*,[1] the Court treats of the promoters as trustees; Lord Cotton, in the same case, deals with them as agents of the company; and Sharswood, J., in the leading case of *Densmore Oil Co.* v. *Densmore*,[2] draws an analogy between the position of promoters in respect of the company, and the relations of partners *inter sese*.

In deciding as to whether promoters were liable to turn over to the company secret profits, he said: "It is a familiar principle of the law of *partnership*, that one partner cannot buy and sell to the partnership at a profit; nor if a partnership is in contemplation merely, can he purchase with a view to a future sale without accounting for the profit." And on this ground he rested the decision.

It is a mistake, however, to suppose that the analogy is perfect as between promoters and either trustees, agents, or partners. Strictly speaking, a promoter is none of these, but occupies a position in respect of which the law imposes certain duties similar to those imposed in the other instances. If one may use the term, it is a quasi-agency or trusteeship.[3] The subject becomes of practical importance only with regard to the suggestion, that the promoters are agents of the company.

It is clear that if a promoter is treated as a technical agent, then the corporation must be held liable for the promoters acts done within the scope of his agency. That there cannot be an agent when no principal is in existence seems equally clear. We shall later have to discuss a line of cases in which it was held that a technical agency exists, but reason and the great weight of authority are against the proposition, and for the present it is sufficient to say that the idea has been thoroughly discredited.[4] The relationship, therefore, between the promoter and the company is that of corporate fiduciary, and is similar in its obligations to that of trustee or agent.[5]

The relationship ceases to exist when the corporation comes into being, though it has been suggested that, even after

[1] 6 Ch. Div. 371 (1877).
[2] 64 Pa. 43 (1870).
[3] Chandler *v.* Bacon, 30 Fed. 538 (1887).
[4] See *infra*, p. 43.
[5] Chandler *v.* Bacon, 30 Fed. 538 (1887).

incorporation, those engaged in placing the stock may still be called promoters.[1]

§ 3. *Relationship of promoters inter sese.*

It is very generally stated in America that the projectors of a company are partners, and that their mutual rights and duties are determined by the law applicable to partnerships.[2] In England, however, the theory obtains that the promoters do not necessarily stand in this relation to each other, though they may do so under certain circumstances. The actual position which they occupy in any given case is a question of fact for the jury.[3]

Under the American rule, it is logically held that one promoter cannot recover from another for anything due on account of the formation of the company, in analogy to the familiar doctrine of partnerships that one partner cannot recover from another for anything due on account of the partnership business.

While the American doctrine thus broadly stated has undoubtedly a just application in certain cases, it must not be taken to mean that anyone who shall have done some act with reference to the formation of the company, and thereby become as to such act a promoter, is the partner of all others who have similarly acted, and therefore liable to be charged for their acts. Such a result would be unjust and could subserve no good purpose. The rule must be understood to provide that all those who act jointly in any transaction or series of transactions with respect to the corporate formation, are, in so doing, partners. The case of *Witmer* v. *Schlatter*[4] was one in which the doctrine of partnership was held applicable. That was an action of assumpsit brought against Schlatter and one hundred and seventy-six others as partners, who under the title of the "Contracting Committee of the Phila. &

[1] Bramwell, J., in Tuycross *v.* Grant, 2 C. P. Div. 503.

[2] Redfield on R. R., p. 11, § 3; Witmer *v.* Schlatter, 2 Rawle, 329 (1831); Roberts Mfg. Co. *v.* Schlich, 64 N. W. 826 (Minn. 1895); Smith *v.* Warden, 86 Mo. 399.

[3] Milburn *v.* Codd, 7 B. & C. 419, s. c. 1 M. & R. 238.

[4] 2 Rawle, 329 (1831). See also Brewster *v.* Hatch, 25 N. E. 505 (1890).

Pittsburgh Transportation Co." were carrying on business intending to become incorporated. They authorized one Harper to enter into a contract with the plaintiff in behalf of the corporation afterwards to be formed. Suit was brought against the individual members and a plea in confession and avoidance entered by some of the defendants.

Gibson, C. J., held: "Against those who pleaded, the record is undoubtedly that all who were alleged to be partners are so in fact; but, although the fact of partnership may be established by the separate admissions of all, it cannot be by the admissions of less than all, for the plain reason that a confession is competent to effect none but him who made it." "We are, therefore, of opinion that the parties to the contract are personally liable; but for the insufficiency of the evidence of partnership as to some of the defendants, a new trial is awarded."

The rule having been misinterpreted, however, the court, in *Railroad Gazette* v. *Wherry*,[1] said: "It cannot be contended that anyone who participates as a projector in the organization of a proposed corporation, can be held individually liable for every contract which any other projector sees fit to make in the name of the contemplated corporation, although such contract is made without the authority, sanction or knowledge of the party sought to be held liable."[2]

It would seem, therefore, that any liability to be charged upon a promoter, for the acts of his fellow promoters, must rest rather upon the principles of agency than of partnership,[3] though wherever the promoters have entered into such relations that the elements of a partnership are present, all the consequences of such a relation follow, and the act of one done within the scope of the undertaking, binds all,[4] and each must act with entire good faith as regards the others.[5] Under any other circumstances, however, there is no relation of

[1] 58 Mo. App. 423 (1894).
[2] See also Johnson *v.* Corser, 25 N. W. 799 (Minn. 1885).
[3] Hurt *v.* Salisbury, 55 Mo. 316 (1874); Beach on Corps., § 159
[4] Brewster *v.* Hatch, 25 N. E. 505 (1890).
[5] Densmore Oil Co. *v.* Densmore, 64 Pa. 43 (1870).

confidence between the promoters, and they may deal with each other at arm's length.[1]

This being so, the distinction attempted to be drawn by some writers between the English and American theories as to the relationship existing between the promoters *inter sese*, would seem to be of little practical importance, as there is a substantial uniformity in the results reached.

§ 4. *Personal liability of promoters for contracts made in the corporate name.*

Having considered the relationship in which promoters stand to the corporation and to each other, it remains to inquire how far they become personally responsible for their acts done, or contracts made, in behalf of the corporation which they have undertaken to create. And, first, it may be taken as self-evident, that where the contract is not in fact made on the faith of the corporation, but with the promoter personally, even though it were intended for the benefit of the future company, the promoter is individually liable; for the engagement is his own.[2]

A corollary to this proposition, is, that where the contract on which a plaintiff is attempting to hold a projector personally liable, was made expressly between the plaintiff and the intended company, the plaintiff assuming the risk that such a company would be formed, and that when it came into existence it would bear the burden, and pay the plaintiff's claim, no responsibility rests upon the promoter.[3]

In *Whitney* v. *Wyman*,[4] the defendant and others, describing themselves as the "Prudential Committee of the Grand Haven Fruit Basket Company," wrote to Whitney stating that the company was partially organized, that certain machinery would

[1] Densmore Oil Co. *v.* Densmore, 64 Pa. 43 (1870).

[2] Ruby Chief Mining Co. *v.* Gurley, 29 P. 668 (Colo. 1892); Perry *v.* Little Rock, Etc., R. R., 44 Ark. 383 (1884); Carmody *v.* Powers, 26 N. W. 801 (1886); Wilbur *v.* N. Y. Co., 12 N. Y. Supp. 456; Heleca Gold Mining Co. *v.* O'Neill, 19 N. Y. Supp. 592.

[3] Whitney *v.* Wyman, 101 U. S. 392. See *contra* (an old case) Furnival *v.* Coombs, 5 M. & G. 736; Landman *v.* Entwistle, 7 W. H. & G. 632.

[4] 101 U. S. 392.

be needed, and ordering the machinery in the name of the company. Whitney addressed his reply to the "Grand Haven Fruit Basket Company," stating that the machinery was in process of construction. The goods were charged on the plaintiff's books to the company, but no payment having been made he sued the members of the committee personally.

Swayne, J., held that there could be no recovery, saying: "It seems to us entirely clear that both parties understood and meant that the contract was to be, and in fact was, with the corporation and not with the defendants individually."

In *Landman* v. *Entwistle*,[1] Parke, B., said: "It is clear that plaintiff undertook to do the work, not upon a contract with the provisional committee, but looking to the chance of the scheme succeeding and of there being funds available for the payment of his claim."[2]

In the absence of any express stipulation of this sort, exempting the promoter from liability, he is responsible for all acts done or contracts made by him or with his authority, though they were so done or made in the name of the corporation;[3] and this is so whether the proposed corporation is never formed,[4] or fails,[5] and even though incorporation were completed and the company had made itself responsible.[6] In the latter case the plaintiff has a choice of remedies against the promoter or the company,[7] for the reason that the action of the company by which it becomes bound is in effect the making of a new contract, and that therefore the original agreement between the plaintiff and the promoter is unaffected.[8]

The cases under this head may be divided into two classes: (1.) Those in which the party contracting with the promoter

[1] 7 W. H. & G. 632.

[2] See also Hersey *v.* Tully, 44 P. 854 (Colo. 1896).

[3] Fredendall *v.* Taylor et al., 26 Wis. 286 (1860).

[4] Johnson *v.* Corser, 25 N. W. 799 (Minn. 1885).

[5] Roberts Mfg. Co. *v.* Schlich, 64 N. W. 826 (Minn. 1895); Hurt *v.* Salisbury, 55 Mo. 316 (1874); Weatherford R. R. *v.* Granger, 24 S. W. 795 (Texas, 1894); Kerridge *v.* Hesse, 9 Car. & Payne, 200.

[6] Queen City Furniture Co. *v.* Crawford, 30 S. W. 163 (Mo. 1895).

[7] Scott *v.* Ebury, 36 L. J. C. P. 161.

[8] Queen City Furniture Co. *v.* Crawford, 30 S. W. 163 (Mo. 1895). See *infra*, p. 49.

believed that the corporation, in whose name the contract was made, was in existence. (2.) Those in which he knew that the corporation was in process of formation only. Let us consider the grounds upon which the promoter's liability rests, in connection with each of these classes separately.

(1.) Where the promoter has not disclosed the inchoate condition of the company in whose name he contracts, he may be held liable for breach of warranty of authority, on the ground that where one contracts as agent he impliedly warrants that he has authority from his principal so to act. To have such authority is manifestly impossible where the principal is not yet in existence.[1] He can also be held liable on the further ground that, "where an alleged principal could not have authorized the contract, then it is plain from the beginning that the contract can have no operation at all unless it binds the professed agent. It is construed accordingly *ut res magis valeat quam pereat*, and he is held to have contracted in person."[2]

(2.) It would seem that it is this latter principle alone which can be applied where the projector has disclosed the incomplete condition of the company, or that fact has become known to the other contracting party through extraneous sources.

§ 5. *Liability for torts.*

Manifestly, promoters should be held liable for torts committed in the formation of a corporation, as in any other transaction, and it has accordingly been held that they are liable in deceit for false representations made to induce subscriptions to stock.[3]

§ 6. *Recapitulation.*

From the foregoing discussion it may be concluded, that while promoters stand in a position of trust towards the company, they are technically neither trustees nor agents, and that unless they expressly stipulate against personal liability on their contracts they will be liable, although said

[1] Bishop on Contracts, § 100; Collins *v.* Wright, 7 E. & B. 301

[2] Pollock on Contracts, * 107.

[3] Gerhard *v.* Bates, 2 El. & Bl. 476.

contracts be made in the name and for the benefit of the proposed corporation, and in spite of the fact that the corporation receives the benefit and assumes the obligation.

PART II.

THEORIES UPON WHICH THE CORPORATE LIABILITY HAS BEEN ENFORCED.

CHAPTER II.

The Company not Liable for Acts of Promoters.

§ 1. *Of the rule generally.*

It may be safely said that the rule is now universally established, that a corporation cannot be bound by the acts of its promoters, *qua* promoters, before it comes into existence. A very carefully considered decision in which this conclusion is reached, and a case typical of the American authorities, is that of *Weatherford, Etc., R. R.* v. *Granger*.[1] The Court there says: "There are some propositions affecting this question upon which the authorities seem to be in substantial accord. A promoter, though he purport to act on behalf of the projected corporation and not for himself, cannot be treated as agent, because the nominal principal is not then in existence; and hence, where there is nothing more than a contract by a promoter in which he undertakes to bind the future corporation, it is generally conceded that it cannot be enforced."

The reason here given is the fundamental one upon which the rule rests, and in view of the unanimity of the decisions upon the point, a further discussion would seem to be unnecessary.[2]

[1] 24 S. W. 795 (Texas, 1894).

[2] In re Empress Engineering Co., 16 Ch. Div. 125 (1880); In re Northumberland Avenue Hotel Co., 33 Ch. Div. 16 (1886); Perry *v.* Little Rock, Etc., R. R. Co., 44 Ark. 383 (1884); Marchand *v.* Loan and Pledge Assn., 26 La. Ann. 389 (1874); Davis & Rankin *v.* Maysville Creamery Assn., 163 Mo. App. 477 (1895); Western Screw Co. *v.* Cousley, 72 Ill. 534 (1874); In re Hereford Iron Works Co., L. R. 2 Ch. Div. 621 (1876); Gunn *v.* Assurance Co., 12 C. B. N. S. 694 (1882); Hawkins *v.* Gold Co., 52 Cal. 513 (1877); Morrison *v.* Gold Co., 52 Cal. 306 (1877); Pittsburgh

It was, indeed, suggested in *M'Dermott* v. *Harrison*,[1] that "the rule that the promoters cannot bind a corporation subsequently to be formed," does not apply to private corporations, but only to those exercising a franchise of a public or *quasi* public character. As the case relied on by the Court as authority for this proposition[2] was a suit between two former promoters of a company, on a contract made with regard to the future management thereof (they being the sole proprietors), and as the company was in no way implicated in the action, and the decision was merely, that such a contract was not illegal as purporting to regulate the action of the intended company, the suggested distinction seems to be without the support of authority. It has not been followed elsewhere.

§ 2. *Rule not applicable where there is a de facto corporation.*

If, instead of a case in which a promoter has acted for an inchoate company, one is supposed in which a *de facto* corporation has acted in its own behalf, the question may arise whether if the body subsequently discovered the defect in its organiza- and completed the quota of the statutory requirements, the duly incorporated company becomes bound by the acts of the *de facto* organization.

It would seem that there can be no objection in theory or

& Tenn. Copper Co. *v.* Quintrell, 20 S. W. 284 (Texas, 1892); Huron Printing Co. *v.* Kittleson, 57 N. W. 233 (S. D. 1894); Schreyer *v.* Co., 43 P. 719 (Oregon, 1896); Stowe *v.* Flagg, 72 Ill. 397 (1874); Weatherford R. R. Co. *v.* Granger, 24 S. W. 795 (Texas, 1894); Arapahoe Co. *v.* Platt, 39 P. 584 (Colo. 1895); Long *v.* Citizens' Bank, 29 P. 878 (Utah, 1892); Battelle *v.* Cement Co., 33 N. W. 327 (Mo. 1887); Buffington *v.* Bardon, 50 N. W. 776 (Wisc. 1891); McArthur *v.* Printing Co., 51 N. W. 216 (Minn. 1892); Joy *v.* Manion, 28 Mo. App. 55 (1887); Hill *v.* Gould, 129 Mo. 106 (1895), *dictum*; Stowe *v.* Flagg, 72 Ill. 397 (1874); Gent *v.* Ins. Co., 107 Ill. 652 (1883); Franklin Fire Ins. Co. *v.* Hart, 31 Md. 60 (1869); Munson *v.* R. R., 103 N. Y. 58 (1886); Heleca Gold Co. *v.* O'Neill, 19 N. Y. Supp. 592 (1892); Rogers *v.* Texas Land Co., 134 N. Y. 197 (1892); Oakes *v.* Cattaraugus Co., 143 N. Y. App. 430 (1894); Burden *v.* Burden, 4 N. Y. Supp. 499; Payne *v.* Coal Co., 10 Exch. 281 (1854); Caledonian R. R. *v.* Helensburg, 2 Macq. H. of L. 393 (1856).

[1] 9 N. Y. Supp. 184 (1890).

[2] Lorillard *v.* Clyde, 86 N. Y. 384.

upon grounds of policy to holding the company liable. The rule under discussion has no application, for it refers merely to corporations not *in esse*. In contemplation of law, however, a *de facto* company has an actual existence as a corporation, and the fulfilment of the formal requisites adds nothing to the corporate vitality, nor does it in any true sense change the constitution or character of the body. The act of one was in all fairness and equity the act of the other. So it has been held that, under such circumstances, the company after due organization, is bound by its previous acts, for the acts are its own and not those of mere promoters.[1]

§ 3. *Company bound where the charter so provides.*

It has been decided, and there are numerous dicta to the same effect, that if the charter provides that a contract made by promoters of a company shall be binding upon it, or if the charter gives to the promoters power to bind the corporation, and they exercise the power so given before organization is completed, then in either event the corporation upon coming into existence will be bound.

The case of *Tilson* v. *Town of Warwick Gas Light Co.*,[2] was an action of debt brought by the attorneys who had obtained the act incorporating the defendant company. The act provided that all costs of procuring it should be paid and discharged by the company. Bayley, J., said: "Now, where an Act of Parliament casts upon a party an obligation to pay a specific sum of money to particular persons, the law then enables those persons to maintain an action of debt," and judgment was thereupon rendered for the plaintiff.[3]

It is to be noted that the Court treats of the obligation of the defendant as one created by statute, and not as resting

[1] Wood *v.* Wheelen, 93 Ill. 153 (1879).

[2] 4 B. & C. 961 (1825).

[3] See also Gent *v.* Merchants Ins. Co., 107 Ill. 652 (1883); Munson *v.* Ry. Co., 103 N. Y. 58 (1886); Preston *v.* R. R. Co., 5 H. of L. 605 (1856); In re Rotheram, L. J. N. S. 219; Low *v.* R. R. Co., 45 N. H. 385 (1864); Ely *v.* Assn., 34 L. T. N. S. 190; Caledonian Ry. Co. *v.* Helensburg, 2 Macq. H. of L. 393 (1856); Touche *v.* Metropolitan Ry. Co., 6 Ch. App. 671 (1870); Hill *v.* Gould, 129 Mo. 106 (1895); Weatherford R. R. *v.* Granger, 24 S. W. 795 (Texas, 1894).

upon the intention of the parties or the circumstances of the case. It is the force of the statute that obligates the company to make payment, although it is the contract made with the promoter that allows the plaintiff to bring his action in debt for a specific sum, rather than in the form of a *quantum meruit*, for the reasonable value of the services rendered. The case does not decide, therefore, that any liability would exist in the absence of statutory provision.

The American cases cited in the note usually treat of the obligation as resting upon the intention of the parties or the circumstances of the case, and give effect to the charter provision merely as allowing a recovery against the company. Such recovery would otherwise be denied, on the ground that the rights of shareholders would be impaired by permitting it, as they had no notice of these claims for services rendered prior to incorporation. The obligation exists under such a view independent of the charter, and there is no objection to enforcing it when the charter has protected the rights of innocent third parties taking stock, by warning them of the incumbrances upon the property which they are about to purchase.

It is held in England that the mention of the contract in articles of association, or even a statement contained therein that one of the objects for which the company is to be formed, is the payment of the plaintiff's claim, do not bind the corporation as do like provisions contained in the charter.[1] It would seem that the distinction drawn must be based upon the fact that the charter being an Act of Parliament is obligatory irrespective of contract, while the articles of association constitute at most only an agreement between the parties to them.

It would seem that from the point of view adopted by the American courts, as to the purpose and effect of such provisions, that articles of association duly recorded according to statute, should put purchasers of stock upon notice of prelimi-

[1] In re Empress Engineering Company, 16 Ch. Div. 125 (1880); Howard *v.* Patent Ivory Mfg. Co., L. R. 38 Ch. Div. 156 (1888); In re Rotheram, L. J. N. S. 219; Ely *v.* Association, 34 L. T. N. S. 190.

nary expenses incurred in the formation of the company, as effectively as would a charter.[1]

§ 4. *Suggestion that company bound where all the projectors have contracted.*

It has been suggested (though what was said in the case was purely dictum) that, where all the stockholders of a corporation were parties to a contract made before organization, the company should be liable in equity upon the contract, on the ground that in substance, at least, the contract was made by the company itself.[2]

This theory, if permissible at all, could only be applied where no strangers to the contract had, subsequent to it, become interested in the corporation; for otherwise those would be charged who had no part in the transaction.[3] Since such a rule overlooks the distinction between the corporation and its members, there would seem little reason for its adoption, and, indeed, it has been expressly repudiated in at least two well-considered cases.[4]

§ 5. *Doctrine that corporation is in esse when charter granted but no organization has taken place.*

It has also been suggested that if, under a general incorporation law, articles of association have been taken out; or if a charter has been granted by legislative enactment, though organization has not taken place thereunder; in either case the corporation is sufficiently formed to be treated as being *in esse*, and may be bound by the acts of a majority of the corporators or promoters.

The idea originated in *Hall* v. *Vermont, Etc., R. R. Co.*,[5] in which case the Court said: "It may be true that the company was not invested with full corporate powers until after the stock was subscribed, and their organization perfected in the

[1] Weatherford R. R. Co. *v.* Granger, 24 S. W. 795 (Texas, 1894).

[2] Paxton *v.* Bacon Mill Co., 2 Nev. 257 (1866).

[3] Chicago Coffin Co. *v.* Fritz, 41 Mo. App. 389.

[4] Battelle *v.* Cement Co., 33 N. W. 327 (1887); Little Rock, Etc., R. R. Co. *v.* Perry, 37 Ark. 164 (1881).

[5] 28 Vt. 401 (1856).

choice of directors; yet the corporation was *in esse* before the event; it had an inchoate existence and the corporators had the power and were so far the agents of the corporation as to bind them by any act which they were required to do, or which was necessary to perfect their organization under the charter."

While the result reached may be entirely justifiable, the grounds on which it proceeds involve considerable difficulty. It would seem that if the services were necessary to the company, and rendered with the expectation of compensation, the law would imply a promise to pay their reasonable value, and there would be no necessity for the Court to make use of the fictions of agency, and of corporate existence before organization.

The rule laid down in this case appeared as a dictum in *Low* v. *R. R. Co.*,[1] where it was said, (after a discussion of the above decision): "If it were true that, at the time the services were rendered, the corporation had no capacity to contract—*which is by no means clear after the charter has been accepted*—still, etc., etc.," and later: "The grantees named in the charter are the sole members of the corporation, until associates are admitted by them; and they may, at a meeting duly called and holden, accept the charter and choose directors and other corporate officers. They may, indeed, proceed to discharge the duties devolved upon the corporation by its charter without the admission of any associates. It is obvious, then, that to bind the corporation by an acceptance of the charter, or other act the concurrence of at least a majority of the grantees or members is necessary."

It will be seen later that in the Pennsylvania case of *Bell's Gap R. R. Co.* v. *Christy*,[2] the Court under a misapprehension of this rule, as laid down in *Low* v. *R. R.*, have confused it with the rule that "a man will not be allowed to unjustly enrich himself at the expense of another," and instead of using the two theories disjunctively, as is done in *Low* v. *R. R. Co.*, have made the consent of a majority of the corporators a pre-

[1] 45 N. H. 370 (1864).
[2] 79 Pa. 54. (1875).

requisite to a recovery in quasi-contract. The same anomalous doctrine is held in the later Pennsylvania case of *Tift* v. *Bank.*[1]

These latter cases, however, need not be further considered at this time, as they are not authorities for the proposition laid down in *Hall* v. *Vermont, Etc., R. R. Co.*; that proposition not having been understood as interpreted in *Low* v. *R. R. Co.*

Suffice it to say, that the rule under discussion has only been enunciated (as far as can be ascertained) in one other case,[2] and is now generally ignored. It has also been expressly denied,[3] and would seem to be out of accord with the general rule, that the corporate franchises remain in abeyance till all the requirements of incorporation are fulfilled.[4]

As to what requirements are essential, and what may be overlooked without causing a fatal flaw in the corporate structure, is a question somewhat foreign to the present discussion; suffice it to say that it has been held (under a general incorporation law) that where the final certificate has been issued, but not properly recorded, the company is *in esse* and bound by its acts.[5]

CHAPTER III.

1. The Former English Equity Rule.

§ 1.

Much of the confusion in thought which is apparent in the decisions upon the subject of corporate liability for the acts of promoters is due, it is believed, to a view formerly entertained in England and originating in the courts of equity, that a company is the successor to its promoters, stepping into their place and assuming all their rights and liabilities. Or, as the thought appeared later in a modified form, if the association of projectors and the corporation are not one and the same body in different stages of existence, the promoters are, at least, agents of the

[1] 141 Pa. 550 (1891).

[2] Harrison *v.* Vt. Manganese Co., 20 N. Y. Supp. 894.

[3] Gent *v.* Ins. Co., 107 Ill. 652 (1883); R. R. Co. *v.* Ketchum, 37 Conn. 170 (1858).

[4] Dartmouth College *v.* Woodward, 4 Wheat. 791.

[5] R. R. Gazette *v.* Wherry, 58 Mo. App. 423 (1893.)

company and can bind it for all purposes of organization. Now though, in these cases, the courts generally declared that the basis of their conclusion lay in the fact that the company had received a benefit and must assume the corresponding burden, they uniformly enforced the contract made by the promoters against the corporation, granting specific performance thereof (without regard to the actuality of the benefits accruing to the corporation), wherever it appeared that the party contracting with the promoter had fulfilled his part of the agreement. It would seem that, unless the Court conceived of the promoters as agents of the company with authority to bind it by contract, specific performance could not have been granted, however just it might be, to hold the company liable for the reasonable value of the plaintiff's land and services.

These cases will be considered at some length, because it is believed that the theory which they advance originated in a misapprehension of authority; and though this has been pointed out and the doctrine repudiated in England, the cases are not infrequently quoted in the American decisions. So far as they are to be taken to lay down the proposition that one cannot be allowed "to unjustly enrich himself at the expense of another," they are not to be questioned, but the results reached disprove the suggestion that this was the only principle invoked.

In the case of *Vauxhall Bridge Co.* v. *Earl of Spencer*,[1] Lord Eldon threw out the suggestion that the withdrawing of opposition to a bill in Parliament might, under certain circumstances, constitute a valid consideration for a contract.

A few years later, the case of *Edwards* v. *The Grand Junction R. R. Co.*[2] came up. Edwards, the complainant, filed a bill praying for an injunction to restrain the defendant company from completing its road until it had complied with the terms of a certain contract entered into with complainant by the promoters. There had been a preliminary organization of the company, and application made for a charter. Edwards and others, trustees of a turnpike company, opposed the bill in

[1] Jacob, 64 (1821); 2 Madd. 356.
[2] 1 M. & C. 650 (1836).

Parliament. In consideration of the withdrawal of this opposition, the preliminary organization agreed that the company should construct and maintain a bridge of certain dimensions across the tracks, for the pike to run over. To enforce this contract against the company the bill was filed.

Lord Cottenham, in delivering the judgment, said: "The objection to the bill rests upon grounds purely technical, and these applicable only to actions at law. The question is not whether there be any legal binding contract at law, but whether the Court will permit the company to use the powers under the act in direct opposition to the arrangement with the trustees before the act, and upon the faith of which they were permitted to obtain such powers. If the company and the projectors cannot be identified, still it is clear that the company have acceded to and are now in possession of all the projectors had before. They are entitled to all their rights and subject to all their liabilities. If any one individual had projected such a scheme and, in prosecution of it, had entered into an arrangement, and then had assigned all his interest in it to another, there could be no legal obligation between those who dealt with the original and such purchaser; but in this Court it would be otherwise. So here, as the company stands in the place of the projectors, they cannot repudiate the arrangement into which such projectors have entered in their corporate capacity; they cannot use the powers given by Parliament to such projectors and refuse to comply with those terms, upon the faith of which all opposition to their obtaining such powers was withheld." The injunction was granted, his lordship resting his decision on the case of *Vauxhall Bridge Co.* v. *Lord Spencer*, which, as we have seen, merely suggested that withdrawing opposition might be good consideration for a contract, but did not even hint that the company would be bound if the contract were made before incorporation.

Here, then, we have the bold annunciation of the theory, unsupported by any adequate authority, that the "company stands in the place of the projectors" and "cannot repudiate the arrangement into which such projectors have entered in their corporate capacity." And his lordship's statement,

"If the company and the projectors cannot be identified," etc., is no qualification of this position, for he goes on to say, "still it is clear that the company have acceded to and are now in possession of all that the projectors had before. They are entitled to all their rights and subject to all their liabilities." This is in effect making the projectors and the company identical, for the conception of the Court seems to be that the company, upon coming into existence, was substituted for the promoters, and that all those contracts which were binding upon the promoters were necessarily obligatory upon the corporation.

In the two later cases of *Stanley* v. *The Chester & Birkenhead R. R. Co.*,[1] and *Petre* v. *Eastern Counties R. R. Co.*,[2] in which the facts were practically the same, Lord Cottenham arrived at similar results upon the same reasoning, both being bills in equity. See also[3]

The doctrine was again advanced in the leading case of *Preston* v. *Liverpool & Manchester R. R.*[4] That was a bill praying specific performance of a contract entered into with the promoters of the company. Two associations were applying for charters to run roads over practically the same route. As only one charter would be granted, it was agreed between them that the successful applicant should assume all contracts made by the other with land-owners. The defendant company obtained the charter. The unsuccessful association had entered into an agreement with Preston for the purchase of his land. The defendant having changed its route somewhat, so that Preston's land was of no use to it, refused to buy or fulfil the contract. Preston filed this bill, to which the defendant demurred.

The Court said: "The doctrine in equity on this subject, where projectors of a company enter into contracts on behalf of a body not existing at the time of the contract but to be called into existence afterwards, is that if the body for whom

[1] 9 Simons, 264, s. c. 3 M. & C. 773 (1838).

[2] 1 Am. & Eng. R. Cas. 462.

[3] St. Leonard's opinion in Hawkes *v.* Eastern Counties R. Y. Co., 4 Eng. L. & Eq. 91 (1851), where other cases are cited.

[4] 7 Eng. Law. & Eq. 124.

the projectors acted does not come into existence, it cannot take the benefit of the contract without performing that part of it which the projectors undertook that it should perform; that is, in substance, this Court treats the projectors for that purpose as agents of the company so afterwards called into existence." The demurrer was, therefore, overruled.

The case was appealed to the House of Lords on the construction of the contract, but was not reported till five years later.[1] In the meantime it was followed both here and in England, and is still very generally cited for the proposition that a corporation comes into existence *cum onere*, the fact having been overlooked, in a large number of instances, that the case was re-argued and a different result reached.

When the case came before the House of Lords on appeal, Lord Chancellor Cranworth said: "The plaintiff's theory is, that the company comes into existence *cum onere*. I am aware that that is a doctrine acted upon by Lord Cottenham. . . . And it has been acted upon in so many cases that it would be very inexpedient offhand to say that that doctrine cannot be sustained, when one considers how much may have been done upon the faith of it. I must, however, own that when the subject comes to be very closely examined, I think there are objections of the gravest nature to its adoption, objections which do not seem sufficiently to have pressed upon the mind of his lordship. Lord Cottenham acted upon this principle that the railroad company was the successor of the projectors or the assignee, if one may say so, of the projectors, and must take existence subject to the burdens which had been contracted for by those who were the promoters of it and to whom it owed its existence. . . . Observe, my lords, to what this doctrine leads. There is that case of Lord Petrie, at which everybody starts when he hears it, in which there was a contract entered into by the projectors of a company that, if Lord P. would withdraw his opposition they would pay him £120,000 for that which was not worth above £4000. It may be that some of those who purchased the shares of that com-

[1] 5 H. of L. 605 (1856).

pany were aware of that contract; but in all probability that was not the case with the majority. If this might be done once, as in the case of Lord P., it might have been done with ten other landed proprietors, and there would have been a million of the capital of the subscribers contracted away from them without any sort of knowledge upon their part and for purposes quite foreign from those for which they subscribed.

If, therefore, this case had turned upon the validity or non-validity of that doctrine, I should have desired of your lordships further time to consider as to the course which was to be taken; but it does not."

The Court then proceeded to construe the contract and came to the conclusion that it was not a contract to pay £5000 for withdrawing opposition, but that plaintiff was to have received this sum if opposition were withdrawn and the land taken. That the taking of the land by the corporation was a condition precedent to its liability. That, as the land had not been taken, the contract fell, and it was not necessary to consider whether or not the corporation would have been bound if the contract had been interpreted differently.

Though the Court avoids expressly overruling the earlier cases, it is apparent from the fact that, by far, the greater part of the opinion is devoted to a stringent criticism of this doctrine promulgated by Lord Cottenham, that their dissent from it was intended to have the weight of authority. The case was argued at length and carefully considered, and the dictum expressed is so strong that it must be considered to have discredited the former rule.

The attitude of the Court upon the subject is even more clearly indicated in the opinion of Lord Brougham: "I have more than doubts of the soundness of those dicta, I may say of those judgments of my noble and learned friend, now no more; I have more than doubts. I think they were carrying very far, indeed, a great deal too far, certain doctrines which had themselves been the subject of dispute."

The specific performance prayed for was therefore refused.

In the same year, 1856, the doctrine was again strongly assailed in the House of Lords, in the case of *The Caledonian*

& Dumbartonshire Junction R. R. v. *The Magistrates of Helensburgh.*[1] The Magistrates contracted with the "Committee of Management" of the proposed company, undertaking to extend the harbor of Helensburgh and erect a quay; the company to pay part of the expenses. The magistrates having performed their part, bring a bill for specific performance, the defense resting on the ground that the company is not bound by the acts of its promoters.

The Court said: The argument of appellee "proceeds on the ground that the Committee of Management ought to be treated in the nature of agents for the company, which owes its existence to their exertions, and when the company came into being it was, from its very birth, bound to fulfil the contracts by which its projectors had stipulated that it should be bound. This reasoning rests on the assumption that a railway company, when established by Parliament is, in substance though not is form, a body succeeding to the rights and coming into the place of the projectors. . . . When such a body applies, however, for incorporation, what they ask for is not an act incorporating themselves only, but all who may be willing to subscribe the specified sums and so become shareholders, and those becoming shareholders have a right to consider that they are entitled to all the benefit held out to them by the act and liable to no obligation beyond those which are there indicated. . . If secret and unexpected terms are to be held binding on those who take shares, the result may be ruinous to those who act on the faith of what appears on the face of the legislative incorporation. . I can discover no principle, legal or equitable, whereby such contracts can be held to be obligatory on the company.'" "In holding that the company is a body different from its projectors in substance as well as form, I am acting on what is the mere truth, and no injustice can arise to those who have dealt with the projectors, for against them and all under whose authority they acted, there will be a clear right of action if the company does not fulfil the engagements which they have contracted that it shall perform, and that is surely all which those who

[1] 2 Macq. H. of L. Cases, 393 (1856).

have dealt with the projectors can claim as their right. For these reasons I am of opinion that on principle there is no ground for holding that a company is bound by any engagement made by those who obtained its act of incorporation, unless those engagements are embodied in the act of incorporation itself." After a careful consideration of all the authorities, the Court goes on to say: "I have stated my reason for thinking that such a doctrine rests on no sound principle and may lead as, in Lord Petrie's case, I think it did lead, to great injustice. And if, therefore, the case now to be decided was in all respects similar to the three cases I have referred to, what I should have to decide would be whether I should advise your lordships to adhere to the precedents established by Lord Cottenham, on the ground that it is unsafe to act against a series of decisions even though they may appear not to rest on any solid foundation, or to depart from them and to adopt what I consider a just and more correct principle." His lordship thereupon differentiated this case from the others on the ground that the contract to pay for erecting a quay and enlarging the harbor, though ultimately for the good of the company, was not within its powers, and that since even a contract made by the directors could not be enforced against the company under such circumstances, certainly one made by promoters could not be.

This decision, like that of *Preston* v. *R. R. Co.*,[1] while avoiding the necessity of overruling the former cases, is unstinting in its condemnation of the theory therein contained, and since its time, the doctrine that a corporation can come into existence subject to burdens imposed upon it by its promoters, has never found credence in England. It has been suggested, indeed, that the case of *Spiller* v. *Paris Skating Rink Co.*,[2] rested upon this ground, but that case came up on demurrer to a bill which charged that the defendant company had acted upon and adopted the contract made for it by its promoters, and that, therefore, the plaintiff was entitled to have the agreement performed. And the Court held, that the demurrer having

[1] 5 H. of L. 605 (1856).
[2] 7 Ch. Div. 368 (1878).

admitted the fact of adoption, the plaintiff was entitled to the relief claimed, and the demurrer was thereupon overruled. The only thing decided, therefore, was that *after* the company came into existence it might voluntarily *adopt* the contract and become bound under it. Whether or not such doctrine be sound, it is an entirely different theory from the one under consideration, for it involves the conception that the obligation rests upon the intention of the company as expressed in its voluntary act, whereas, in Lord Cottenham's view the corporation enters upon its existence, *cum onere*.

§ 2. *Not applicable at law.*

It has been asserted[1] that this doctrine was, in England, of general applicability and in vogue both in courts of law and equity, and Mr. Redfield, in support of this proposition, cites the case of *Howden* v. *Simpson*.[2] That was an action of debt brought by Lord Howden against Sir John Simpson and others, formerly projectors of a railroad company, upon an instrument, under seal, in which the defendants had agreed to pay the plaintiff £5000 for withdrawing his opposition to a bill granting a charter to the railroad. The only question involved was whether or not such a contract was legal, in view of the fact that Lord Howden was a member of Parliament at the time. No attempt was made to hold the company, so that the case does not support the proposition advanced.

Pointing to a contrary conclusion is the case of *Payne* v. *Coal Co.*[3] Promoters of the coal company, after provisional, but before complete registration, promised the plaintiffs that if they would give up their plan of organizing a similar company, they would see that plaintiffs should be made ship brokers for the defendant company when formed, and that said company would give plaintiffs a free passage to Australia. Assumpsit for breach of contract, in that the company refused so to do, though plaintiffs had performed their engagement in the matter.

[1] Redfield on Railroads, 5 Ed. p. 25.
[2] Keen, 583, 3 M. & Cr. 97, 10 Ad. & Ellis, 793, 9 Cl. & F. 61.
[3] 10 Exch. 281 (1854).

Platt, B., said, "I am clearly of opinion, that it was beyond the power of the provisionally registered company to bind the completely registered company by entering into the contract." This decision denies the applicability of the so-called equity doctrine of *cum onere*, to cases at law, at a time when that doctrine was at its height in the courts of equity, and it seems probable from the statements made in *Melhado* v. *Porto Algere Co.*,[1] and *Spiller* v. *Paris Skating Rink Co.*,[2] that the distinction in this respect between the two jurisdictions was always maintained.

The cases discussed in criticism of this doctrine, have dwelt largely upon the unfortunate practical results which would follow its adoption, the underlying thought being that if a company could be saddled with all the undertakings of its projectors, it would be brought into being, (through the incompetency or unscrupulousness of the promoters), in a condition unfit for the transaction of business, with the capital stock diminished or exhausted, and the stockholders (who could have had no notice of the transaction prior to incorporation) left without any adequate return for their money.

The doctrine seems also open to criticism on more theoretical grounds. It requires that the promoters be conceived of in one of two characters. Either as being in substance the corporation itself, as was suggested in the earlier cases on the subject, or as being agents of the company with power to bind it. It is clear that the conception in either case would be a pure fiction. That a corporation has no existence till it has received legislative sanction in some form or other, is well settled,[3] and it is a mere truism when one says that any body of persons applying for such legislative sanction in the form of a charter can, under no circumstances, be the corporation which they are endeavoring to create. Unless they are conceived of as, in fact, the same body, the conclusion that the corporation stands in the same position as the promoters with all their rights and subject to all their liabilities would seem to

[1] L. R. 9 C. P. 503 (1874).
[2] 7 Ch. Div. 368 (1878).
[3] Thompson on Corps., § 35.

be untenable. Again, it is well established that the corporation is distinct from the sum of its members,[1] so that what they might do in their individual capacities should not on theory bind the distinct and subsequently created company. This view is undoubtedly the one now generally adopted both in England and in this country.[2]

The theory of agency is equally untenable, for the correlative of "agent" is "principal" and there being no principal in existence the relationship cannot exist; and this is now uniformly acknowledged.[3]

Except as a fiction, therefore, this doctrine that a company can be bound before it is formed, and enters upon its corporate life "*cum onere*," must be considered unfounded in principle. As a fiction, the cases have shown that it works deplorable results. It is discredited in England, and has not been followed (as far as can be ascertained) since the decision in *Caledonian R. R. Co.* v. *Helensburgh*.[4] The American authorities repudiate it.[5]

There seems, then, to be no longer any distinction, either here or in England, between the doctrines existing in the law and equity courts. But though the doctrine has been abandoned in its original form, the thought has not entirely passed away in America, that a relationship of agency exists between the promoter and the corporation.

[1] Thompson on Corp., §§ 1–3.

[2] Battelle *v.* Cement Co., 33 N. W. 327 (Mo. 1887); Munson *v.* R. R. Co., 103 N. Y. 58 (1886); In re Northumberland Avenue Hotel Co., 33 Ch. Div. 16 (1886); In re Empress Engineering Co., 16 Ch. Div. 125 (1880).

[3] Schreyer *v.* Turner Co., 43 P. 719 (Oregon, 1896); Weatherford R. R. Co. *v.* Granger, 24 S. W. 795 (Texas, 1894); Long *v.* Bank, 29 P. 878 (Utah, 1892); Battelle *v.* Cement Co., 33 N. W. 327 (Mo. 1887); Buffington *v.* Bardon, 50 N. W. 776 (Wisc. 1891); Joy *v.* Manion, 28 Mo. App. 55 (1887); Davis *v.* Maysville Creamery Assn., 63 Mo. App. 477 (1895); Huron Printing & Binding Co. *v.* Kittleson, 37 N. W. 233 (S. D. 1884); Pittsburgh Copper Co. *v.* Quintrell, 20 S. W. 248 (Texas, 1892).

[4] 2 Macq. H. of L. 393 (1856).

[5] Cases cited, ante, p. 26.

CHAPTER IV.

RATIFICATION.

§ 1. *On theory, ratification inapplicable in order to charge a corporation for acts prior to incorporation.*

It will have been noticed, in discussing the cases on this subject, that the courts frequently use the term "ratification;" indicating that a corporation may, by ratifying a contract made by its promoters, become liable to perform its terms, though the contract was made before it came into existence.

Ratification is a term originating in the law of agency, which may be used with its scientific intendment, when saying that the act of an agent, or the act of one holding himself out as an agent, has been ratified. It is "an agreement to adopt an act performed by another for us," and is either express or implied.[1] But that there may be a ratification in a technical legal sense, the one purporting to ratify an act must have been in existence at the time the act was done,[2] for in theory this adoption of an act done by another is only possible because the act was done on our behalf, and it cannot be said in any true sense that an act was done on behalf of a person not *in esse*.

As is said by Pollock:[3] "When a principal is named or described, but is not capable of authorizing the contract so as to be bound by it at the time, there can be no binding ratification, for ratification must be by an existing person on whose behalf a contract might have been made at the time."

It is difficult to perceive, therefore, how this doctrine of agency can be applied, (with any due regard to an exact use of scientific terms,) in order to charge a corporation for having knowingly taken the benefit of a contract made before its existence commenced. The better opinion seems to coincide with this view, and in the leading case of *Kelner* v. *Baxter*,[4] Willis,

[1] Bouvier's Law Dictionary.
[2] Anson on Contracts, * 335–36; Chitty on Contracts, p. 293.
[3] Contracts, * 107.
[4] L. R. 2 C. P. 175 (1866).

J., said: "Could the company become liable by a mere ratification? Clearly not. Ratification can only be by a person ascertained at the time of the act done, by a person in existence either actually or in contemplation of law, as in the case of the assignees of bankrupts, or administrators whose title for the protection of the estate vests by relation."

The cases denying the applicability of the doctrine of ratification are numerous, and would seem to have the weight of reason and authority,[1] for, under the circumstances, privity of contract is impossible.

It is, nevertheless, true that the doctrine of ratification has been made use of in a number of cases,[2] and where it is employed it would seem that the rule of agency, (that where a contract is ratified, the agent, if he has contracted as such, is relieved from responsibility,) is invoked to discharge the promoter of personal liability on the contract. Such, at least, was the intimation in *Whitney* v. *Wyman*,[3] though we have seen that ordinarily the rule is otherwise.[4]

In *Buffington* v. *Bardon*[5] the laxity of thought which an adoption of this theory necessitates is clearly brought out. That was an action by Buffington to charge the defendants, as stockholders of a corporation, upon a contract which plaintiff alleged that he made with the company. The lower Court instructed the jury that, before they could render a verdict for the plaintiff, they must find that the corporation promised to pay the plaintiff for his services, or that after it was organized the corporation or its authorized agents, know-

[1] Melhado *v.* Porto Alegre R. R. Co., 9 C. P. 503 (1874); In re Empress Engineering Co., L. R. 16 Ch. Div. 125 (1880); Weatherford R. R. *v.* Granger, 24 S. W. 795 (Texas, 1894); McArthur *v.* Times Co., 57 N. W. 216 (Minn. 1892); Gunn *v.* Assurance Co., 12 C. B. N. S. 694 (1862); In re Northumberland Ave. Hotel Co., 33 Ch. Div. 16 (1886).

[2] Carey *v.* Des Moines Coal Co., 47 N. W. 882 (Iowa, 1891); Bruner *v.* Brown, 38 N. E. 318 (Ind. 1894); Buffington *v.* Bardon, 50 N. W. 776 (Wisc. 1891); Stanton *v.* R. R. Co., 59 Conn. 272 (1890); Paxton Cattle Co. *v.* Bank, 21 Neb. 621 (1887); Hill *v.* Gould, 129 Mo. 106 (1895). Dictum.

[3] 101 U. S. 392 (1879).

[4] Ante, p. 24.

[5] 50 N. W. 776 (Wisc. 1891).

ing all the facts, adopted the services and made use of the same. Verdict was rendered for plaintiff. Lyon, J., held, "The law is that a corporation is liable for its own acts only after it has a legal existence. Until that time no one, whether a promoter or not, can sustain to the corporation the relation of agent. Were this not so, we would have an agent without a principal, which is an absurdity. But if one assumes to act as agent for a prospective corporation, and in form enters into a contract in its behalf, it is competent for such corporation, when organized, to ratify such contract. If with full knowledge of all the facts, but not otherwise, the corporation assumes the contract and agrees to pay the consideration, or accepts the benefit of the contract it will be bound thereby."

Though the language of the lower Court was referred to as being correct, judgment was reversed on the ground that there was no evidence which could have been submitted to the jury tending to prove a ratification with knowledge of all the facts.

While the learned judge in this case justly characterizes as absurd the theory that the promoters are agents of the company, it would seem that he has fallen into a like mistake when he boldly asserts that the technical theory of ratification is applicable to a case in which, as he admits, there is no relation of principal and agent and no principal in existence for whom anyone might assume to act as agent.

§ 2. *Where doctrine recognized, knowledge of facts a prerequisite to liability.*

Where the doctrine is employed, however, one of the prerequisites should be, as the above case lays down, that the corporation must have had knowledge of all the material facts and circumstances of the transaction which it is charged with having ratified, for otherwise, according to the law of agency, no ratification is possible.[1] This rule is recognized in the cases.[2]

[1] Story on Agency, § 239.

[2] Stanton *v.* R. R., 59 Conn. 272 (1890).

§ 3. *Only acts within scope of the corporate powers can be ratified.*

It is also laid down that only acts within the scope of the corporate powers can be ratified.[1] Under the doctrine of "special capacities," according to which any act done without the scope of the powers conferred upon the corporation, is no act, (for there was no power with which to act,) this statement would be literally true. The corporation could not ratify a transaction which was beyond the powers granted, for it has not the inherent force so to do. As a corporate act, ratification could not take place.

But since ratification is purely a question of fact depending in any given case upon the intention of the parties as manifested by their acts and words, ratification is physically possible (if the expression may be permitted) and the above proposition must not be understood in any such sense as that the act of ratification is one implied by law, and that the law will not raise the implication where the act, if done by the corporation, would have been *ultra vires*.[2]

§ 4. *Ratification relates back.*

Ratification, as we have seen, is the adoption of an act previously done by one who was, in fact, agent for the ratifier, or who assumed to act as agent for one who was in existence at the time. It follows, therefore, that ratification relates back to the time of the act, and the principal is bound or acquires rights as of that date;[3] *omnis ratihabitis retrohabitur*. So the obligation binding a corporation, which has ratified a contract made by its promoter, dates as of the time of the original agreement.[4] It is the adoption of the old contract, not the making of a new one.

[1] Stanton *v.* R. R., 59 Conn. 222 (1890); Munson *v.* R. R. Co., 103 N. Y. 58.

[2] Oakes *v.* Cattaraugas Water Co., 143 N. Y. App. 430 (1894); Howard *v* Patent Ivory Mfg. Co., L. R. 38 Ch. Div. 156 (1888).

[3] Kelner *v.* Baxter, L. R. 2 C. P. 174 (1866).

[4] Stanton *v.* R. R., 59 Conn. 272 (1890); Negley *v.* Lindsay, 67 Pa. 218 (1872); Low *v.* R. R. Co., 45 N. H. 370 (1864).

§ 5. *What acts constitute a ratification.*

As to what constitutes a ratification, it need only be said that the same rules apply in these cases as in those where the term is more truly applicable. It may be express, or implied from carrying out the terms of the contract or acting with reference to it.

CHAPTER V.

ADOPTION.

§ 1. *Conceived of as the adoption of an old contract.*

Many cases, while denying that there can be in any exact sense a ratification, assert that a company may become bound by adoption.[1] This is not a "term of art;" there is no recognized legal principle so-called, and it is to a consideration of what is meant by the courts when they say that a corporation may adopt the contract and become bound thereby, that we must now proceed.

An examination of the cases would seem to indicate that the term has been used in two distinct senses. In some it has signified, as the word itself denotes, an adoption of a previously formed contract; the assumption by the corporation of the rights and liabilities created by a contract made between a promoter and a third person. In others, the Court has shown, either expressly or by implication, that it meant by "adoption" the making of a new contract with the same terms as the old.

The former of these conceptions was undoubtedly in the mind of the Court in the case of *Rogers* v. *Land Co.*[2]

[1] Pittsburgh *v.* Quintrell, 20 S. W. 284 (Tenn. 1892); Huron Printing Co. *v.* Kittleson, 57 N. W. 233 (S. Da. 1894); Schreyer *v.* Turner Flouring Mills, 43 P. 719 (Oregon, 1896); Weatherford R. R. Co. *v.* Granger, 24 S. W. 795 (Texas, 1894); Colorado Land & Water Co. *v.* Adams (Colo. 1894); Arapahoe Ins. Co. *v.* Platt, 39 P. 584 (Colo. 1895); Battelle *v.* Cement Co., 33 N. W. 327 (Mo. 1887); McArthur *v.* Printing Co., 51 N. W. 216 (Minn. 1892); Pratt *v.* Oshkosh Co., 62 N. W. 84 (Wisc. 1895); Munson *v.* R. R., 103 N. Y. 58 (1886); Burden *v.* Burden, 4 N. Y. Supp. 499 (1896); Touche *v.* Metropolitan Co., 6 Chan. App. 671 (1870); Bommer *v.* American Spiral Hinge Co., 81 N. Y. 469 (1880); Pa. Match Co. *v.* Hapgood, 141 Mass. 145 (1886).

[2] 34 N. Y. 197 (1892); Spiller *v.* Paris Skating Rink Co., 7 Ch. Div. 368 (1878); Match Co., 62 N. W. 84 (Wisc. 1895); 15 Law & Eq. 596 (1852).

A number of persons holding a large tract of land agreed to form a company whose sole purpose should be the disposal of the land in question. Each should contribute his proportion of the land to the company, receiving in return script to represent shares in the company, which should be retired as fast as the company disposed of the land.

When the company was created, instead of paying off the script it declared a dividend to the scriptholders. The suit was brought by one of the scriptholders to compel the payment to be made to the retirement of the script.

Vann, J., held: "By accepting title to the land, it (the corporation) adopted and ratified the agreement entered into by all its stockholders and thereby voluntarily made itself a party thereto and became bound thereby," and the Court thereupon ordered that the agreement between the original owners was binding upon the company and that profits must therefore, be applied to retiring the script. See also[1]

When this is understood, by "adoption" it is manifest that there is little or no distinction to be drawn between it and "ratification" as the latter term is employed in this connection. In their exact signification, adoption denotes the taking to one's self of that with reference to which there existed no prior relation; ratification, the confirmation of an act done without due authority on behalf of an existing principal. But when the term ratification is made use of in a case in which no relationship of principal and agent exists, then, according to the definitions given, there is nothing left whereby to distinguish the two processes. Whatever constitutes a ratification in this sense constitutes also an adoption, and the terms may be used as synonymous. See[2]

This conception seems to be open to the objection that the law of contract does not permit of a stranger substituting

[1] Oakes *v.* Cattaraugas Water Co., 143 N. Y. App. 430 (1894); Pratt *v.* Oshkosh, 62 N. W. 84 (Wisc. 1895); Gooday *v.* Colchester & Stour Valley Ry. Co., 17 Beavan, 132 (1852); Touche *v.* Metropolitan Ry. Co., 6 Ch. App. 671 (1870).

[2] Perry *v.* Little Rock R. R. Co., 44 Ark. 383 (1884); Schreyer *v.* Turner Flouring Mills Co., 43 P. 719 (Oregon, 1896); McArthur *v.* Times Printing Co., 51 N. W. 216 (Minn. 1892).

himself for one of the original parties to a contract except by an agreement between all of the parties concerned, based upon a sufficient consideration. This is on the familiar principle that liabilities cannot generally be assigned.[1]

Now, if we suppose a case in which the corporation has so acted after coming into existence, that under the decisions we are discussing a Court would say that there had been an adoption of the contract, would it not be a mere fiction unsupported by the facts for the Court to imply that the minds of the parties had met and agreed upon the substitution of the liability of the corporation for that of the promoter?

Yet by such mutual agreement alone, according to the law of contract, can a substitution of liabilities take place.

But admitting that a Court would be justified in giving effect to such a substitution on the ground of an implied agreement between the parties to that effect, we are not aided in understanding these decisions, for in none of them does the Court seem to base its result on the reasoning indicated. Indeed, they appear to repudiate it, for such a substitution is, in the words of Anson,[2] "the rescission by agreement of one contract and the substitution of a new one in which the same acts are to be performed by different parties," but the cases under consideration all take the view that the contract binding the corporation is not a new one, but is the old agreement adopted, dating back and taking effect as of the time of the original contract.

A number of cases, however, expressly repudiate the idea and hold that there can be no adoption of the original contract or liability assumed by the corporation under it; and the view may be considered discredited.[3]

§ 2. *The making of a new contract.*

The better opinion as to the nature of this so-called "adoption" is, that it is the making of a new contract between the corporation and the person with whom the promoter con

[1] Anson, Part III., Chapter II.

[2] Contracts, p. 287.

[3] Abbott *v.* Hapgood, 150 Mass. 248 (1889); R. R. Co. *v.* Sage, 65 Ill. 328 (1872); Western Screw Co. *v.* Cousley, 72 Ill. 531 (1874).

tracted, and since it is usually implied from the actions of the company with reference to the promoter's contract, it is generally found that it was the intention of the parties to follow the terms of the original agreement. Hence the rule laid down in the cases, that adoption, is "the making of a new contract with the same terms as the old."[1]

The distinctions taken between the theories of "ratification," "adoption" (understood in its *prima facie* significance), and "adoption" (understood as the making of a new contract), are rather of theoretical than of practical importance in the majority of cases. They become useful, however, wherever the Statute of Frauds or of Limitations is involved. An example of this is the case of *McArthur* v. *Times Printing Co.*[2] That was an action for damages for breach of contract. Promoters of the company had employed plaintiff in behalf of the company as advertising agent for the period of one year from and after October 1st. Plaintiff commenced to render his services on that day, though incorporation was not complete. He continued in the same employment for some time after the company was formed, but was discharged within the year. All the officers and directors knew the terms of the contract, and plaintiff had been paid accordingly, but no formal action had been taken by the company, recognizing the contract.

One of the grounds of defense was that the contract was void on account of the Statute of Frauds, there being no memorandum in writing, and performance not being provided for within the year.

Mitchell, J., held: "This Court, in accordance with what we deem sound reason as well as the weight of authority, has held that, while a corporation is not bound by engagements made on its behalf by its promoters before its organization, it may, after its organization, make such engagements its own contracts, . . . What is called adoption in such cases is, in legal effect, the making of a contract of the date of the adop-

[1] In re Empress Engineering Co., 16 Ch. Div. 125 (1880); Northumberland Ave. Hotel Co., 33 Ch. Div. 16 (1886); McArthur *v.* Times Printing Co., 51 N. W. 216 (Minn. 1892).

[2] 51 N. W. 216 (Minn. 1892).

tion, not as of some former date." Since the contract was adopted, and since it was not made by the corporation until October 16th, and was to last for one year from October 1st, according to the terms of the original agreement, it was to be performed (as far as the corporation was concerned) within the year, and the statute had therefore no application. See also[1]

When it is said that the new contract is made with the same terms as the old, it is apparent that if we are dealing with an actual contract, implied from the circumstances of the case and based upon the intention of the parties, the statement must be taken to embody the results reached in the majority of cases and cannot be understood as a conclusion of law, universally applicable. Though the jury might find, in a given case, that the corporation had undertaken *in toto*, according to the terms of the promoter's contract, such a circumstance would be purely accidental.

In the case of *Standard Printing Co.* v. *Democrat Pub. Co.*,[2] suit was brought by the latter for work done in publishing a paper for the former. The contention was as to the sum due. Plaintiff had previously done the work for former owners of the paper at a certain price. These proprietors had formed the defendant company and turned the paper over to it, the plaintiff continuing to do the work. Nothing was said as to the price. Plaintiff claims that the original agreement should be the measure of his recovery. The *Trial Court* found "that the work was done upon an implied promise that the plaintiff should be paid for it such sum as it should be reasonably worth."

Newman, J., held: "This (the original agreement) was but evidence, more or less persuasive, upon the question what was the agreement upon which the work was done for the defendant. And it was a serious question whether the Court ought to infer a promise by the defendant to abide by the previous contract of the promoters however clearly established."

[1] In re Empress Engineering Co., 16 Ch. Div. 125 (1880); Howard *v.* Patent Ivory Mfg. Co., L. R. 38 Ch. Div. 156 (1888); Northumberland Ave. Hotel Co., 33 Ch. Div. 16 (1886); Battelle *v.* Cement Co., 33 N. W. 327 (Mo. 1887).

[2] 58 N. W. 238 (Wisc. 1894).

The thought that circumstances may contradict the implication arising in any given case (that the corporation intended to contract according to the terms of the promoter's agreement,) was carried to a considerable length, *In re Northumberland Avenue Hotel Co.*[1] Lopes, J., there said: "No doubt the company, after it came into existence, might have entered into a new contract upon the same terms as the agreement of July 24, 1882, and we are asked to infer such a contract from the conduct and transactions of the company after it came into existence. It seems to me impossible to infer such a contract, for it is clear to my mind that the company never intended to make any new contract, because they firmly believed that the contract of July 24th was in existence and was a binding valid contract."

§ 3. *Formal requisites.*

As in those cases which proceed upon the theory of ratification, so in these dealing with adoption, it is held that only acts within the scope of the corporate powers, and such as are not against law or public policy, can be adopted;[2] and that the company must have had knowledge of all the facts before it will be bound.[3]

The question as to who may bind the company by adopting the contract is purely one of agency, to be decided in each case as it arises, and is dependent upon the character of the agreement and the purposes of the corporation.[4]

CHAPTER VI.

ESTOPPEL.

§ 1. *When applicable.*

Besides the theories which we have been considering, another doctrine, that of estoppel, has at times been employed in order

[1] 33 Ch. Div. 16 (1886).

[2] Schreyer *v.* Turner Flouring Mills Co., 43 P. 719 (Oregon, 1896); Munson *v.* R. R. Co, 103 N. Y. 58 (1886); Burden *v.* Burden, 4 N. Y. Supp. 499 (1896); McArthur *v.* Times Printing Co., 51 N. W. 216 (Minn. 1892).

[3] Schreyer *v.* Mills Co., 43 P. 719 (Oregon, 1896); Weatherford R. R. *v.* Granger, 34 S. W. 793 (Texas, 1894); Huron *v.* Kittleson, 57 N. W. 234 (S. Da. 1894); Rogers *v.* Land Co., 134 N. Y. 197 (1892).

[4] McArthur *v.* Times Printing Co., 51 N. W. 216 (Minn. 1892).

to charge a corporation for work done and services rendered in its formation, or upon a contract made by its promoters.

That the liability of the corporation in such cases depended on estoppel was the thought of the Court in the case of *Grape Sugar & Vinegar Mfg. Co.* v. *Small.*[1] That was an assumpsit brought by Small against the company on account of a balance due for work done and materials furnished to the appellant. It was shown that one Sim, acting as president of the company but before it was duly incorporated, had employed plaintiff to build and repair certain "tubs," the employment having lasted till after incorporation. The defendant asked the Court to charge "that plaintiff is not entitled to recover for the work done and material furnished prior to the day on which the certificate of incorporation was filed for record." This the Court refused to do, and there being a verdict for the plaintiff the company took an appeal.

The Court, in affirming the judgment, said: "If, after its incorporation was complete, the company accepted the work done under the contract, it will be estopped, both in law and equity, from denying its liability on account of the same. In other words, the appellant will not be permitted to accept the work done and material furnished by the plaintiff under a contract made prior to the recording of the certificate and, at the same time, deny its liability under it."

In *Weatherford, Etc., R. R. Co.* v. *Granger*[2] the Court, in referring to the corporation, uses the following language: "Having exercised rights and enjoyed benefits secured to it by the terms of a contract made by its promoters in its behalf, a corporation should be estopped to deny its validity." See, also, to the same effect:[3]

Now it will be noticed that, in the case of *Grape Co.* v. *Small*, just cited, the services of the plaintiff had been rendered partly before but partly after complete organization of the company. It had allowed the plaintiff to continue making and repairing

[1] 40 Md. 395 (1874).

[2] 24 S. W. 795 (Texas, 1894).

[3] Joy *v.* Manion, 28 Mo. App. 55 (1887); Low *v.* R. R., 45 N. H. 375 (1864); Thompson on Corp., § 490.

its tubs, with full knowledge that he was doing so under the impression that the company would pay him *according to the terms of the contract*, not only for what he was now doing *but for what he had already done*. Under such circumstances the doctrine of estoppel might have a legitimate application.

§ 2. *When inapplicable.*

But it is submitted that the language used in *Weatherford R. R. Co.* v. *Granger* (and the other cases cited) is too broad, since it would include all cases in which benefits had accrued to a corporation, as well before as after it had come into existence. Now, as to all services rendered or goods bestowed upon a company before it is incorporated it would seem that, if any liability arises, it cannot be based upon the theory of estoppel, for the essential elements of an estoppel are absent.

The elements of an equitable estoppel, by conduct or in *pais*, are laid down in Bispham's Equity.[1] It is there said, "Equitable estoppel or estoppel by conduct has its foundation in fraud considered in its most general sense." There must be an intentional inducing of another to act, with a full knowledge of all the facts, and the other must have acted to his detriment.[2]

It would seem impossible to predicate fraud of a corporation in respect of benefits conferred upon it while in an inchoate condition, and before it had a legal existence.

Again, though the cases suggest that the fraud which estopped the corporation from denying its liability, consists in enjoying the benefits which it knows have been conferred in the expectation that they will be paid for, we have seen that to constitute an estoppel, the one alleging it, must have been induced to act to his disadvantage by the wrong of another, and it would seem to be a strained construction of the doctrine, to hold that a corporation, by merely making use of advantages of which it found itself in possession upon its birth, had induced the conferring of those advantages upon itself.

[1] § 282.

[2] Bispham's Equity, Chap. IV.

PART III.

THE BASIS OF CORPORATE LIABILITY FOR PROMOTERS' ACTS.

CHAPTER VII.

WHERE THE BENEFITS HAVE BEEN CONFERRED AFTER INCORPORATION.

§ 1. *General considerations: A true contract possible.*

It is apparent from the foregoing examination of the cases that in theory, at least, the courts have differed widely as to the grounds of corporate liability. It has been alleged on the one hand and controverted on the other that a company comes into existence burdened with liabilities; the doctrines of estoppel and of ratification have been suggested as theories upon which the corporation might be charged for the benefits received; and, finally, it has been generally conceded that the company may assume liability by a process of adoption, though as to the full effect and meaning of "adoption" there is still some doubt.

Whatever the language used, however, it is clear that the courts have recognized the equity existing against a corporation in respect of advantages of which it has been the recipient under a contract made by its promoters. This equity is recognized in spite of the fact that on strict principle the promoter is the only one who can be liable on the original contract, in view of the non-existence of the corporation at the time the contract was made.

Notwithstanding the diversity in the terminology employed, there is a manifest uniformity in the major part of the results reached, which suggests that the underlying principles are the same in most of the cases.

It remains, then, to consider what are the underlying principles referred to, and how far they have been recognized by the courts. For the purposes of this examination all the cases may be divided into three classes:

First. Those in which the promoters have contracted for the

corporation in respect of something to be done for it after it shall have been duly incorporated.

Second. Those in which the duties to be performed under the contract commence before, and continue after, incorporation.

Third. Those in which the contract has been fully performed and the corporation has received the benefit before it was legally *in esse*.

In cases of the first class where a corporation has been fully organized and, knowing the terms of a contract made between its promoters and a third party, allows the latter to render the services contracted for under the belief that the company intends to pay him for them, we have all the elements of a real contract; a contract implied in fact. The concensus of opinion of all reasonable men would be that the company must have intended to contract according to the terms of the former arrangement, and that in view of its conduct it could not be heard to deny that this was its intention. It is in such a case, and in such a case alone, that the doctrine of estoppel would be applicable.

§ 2. *The promoter's contract a continuing offer to the company.*

In these cases we should expect to find the courts acting on the hypothesis of a true contract and endeavoring to enforce an agreement corresponding to the intention of the parties. So it is usually held that a contract made with a promoter constitutes an open or continuing offer to the corporation, which that body may accept upon coming into existence.[1] Having accepted or adopted this offer either expressly or as is more generally the case, by implication, a contract is formed ordinarily of the same terms as the former one and binding upon the corporation.

As was said in *Penn Match Co.* v. *Hapgood*:[2] "The power of a corporation to make contracts can be exercised in accepting and adopting proposed contracts made in its name and behalf before incorporation. Such a contract must derive its

[1] Pratt *v.* Oshkosh Co., 62 N. W. 84 (Wisc. 1895).

[2] 141 Mass. 145 (1886).

vitality from the meeting of minds when both parties are in existence; until then it can be nothing more than an offer by one party."

The thought was expressed even more fully in *Weatherford R. R. Co.* v. *Granger*:[1] "Again, where the promoters of a corporation have made a contract in its behalf to be performed after it is organized, it may be deemed a continuing offer on the part of the other party to the agreement, unless withdrawn by him, and may be accepted and adopted by the corporation after such organization; and the exercise of any right, inconsistent with the non-existence of such contract, ought to be deemed conclusive evidence of such adoption."

This fiction of the continuing offer would seem to be justifiable as an aid in giving effect to the intention of the parties.

That in these cases we are dealing with true contracts seems to be thoroughly established. In *Howard* v. *Patent Ivory Mfg. Co.*,[2] the company, being duly organized, received the transfer of a leasehold under an agreement made before its existence by its promoters. It knew the terms of the agreement and had passed a resolution undertaking to carry them out. It was argued that, according to an earlier case,[3] the terms of the original contract were not binding upon the company, though it might be liable to pay a reasonable sum for the use of the property.

Kay, J., said: "In the first place I must observe that the question whether there was a contract between this company and Mr. Jordan is a question not of law but of fact. Am I bound, because in one case the Court upon evidence before it came to the conclusion as a matter of fact that there was no binding contract, to hold that in this case there was no such contract?" and judgment was rendered for the plaintiff.

In *Oakes* v. *Cattaraugas Water Co.*,[4] the promoters con-

[1] 24 S. W. 795 (Texas, 1894).
[2] L. R. 38 Ch. Div. 156 (1888).
[3] In re Northumberland Avenue Hotel Co., 33 Ch. Div. 16 (1886).
[4] 143 N. Y. App. 430.

tracted with Oakes that the company should pay him $1000 if he should render certain services. After incorporation the president, who was one of those who made the original agreement, requested Oakes to perform the services. Having done so, the company refused to pay the $1000. The lower Court non-suited plaintiff when he sued for the contract price.

The Court, after suggesting that the parties could make a contract on the same terms as the original one if they were so minded, said: "Whether this was the intention and purpose of the president and of the defendant, and of the plaintiff, was under the circumstances of the case a question of fact which should have been submitted to the jury. Ratification or adoption, which in this case mean the same thing, is legally a question of intention to be determined from facts and circumstances as one of fact, and the Court was not warranted under the circumstances in disposing of the question as one of law." Judgment was, therefore, reversed. See also[1]

Since we are dealing with an obligation founded upon the intention of the parties, certain elements must be present before a jury would be warranted in finding that the undertaking had been entered into by the corporation. First of these is knowledge of the facts and circumstances attending the rendering of the services. This we have seen to be a prerequisite, while discussing the theories separately, and the same reason applies wherever there is a contract implied in fact, for it is impossible to say that one has either ratified or adopted a contract or accepted an offer, when he had knowledge neither of the one nor the other.[2]

If a case should arise in which benefits were conferred upon a corporation after due organization without its knowledge

[1] Rogers *v.* Land Co., 134 N. Y. 197 (1892); Penn Match Co. *v.* Hapgood, 141 Mass. 145 (1886); Pratt *v.* Oshkosh Match Co., 62 N. W. 84 (Wisc. 1895); Standard Printing Co. *v.* Democrat Pub. Co., 58 N. W. 238 (Wisc. 1894); Spiller *v.* Paris Skating Rink Co., 7 Ch. Div. 368 (1878); Northumberland Avenue Hotel Co., 33 Ch. Div. 16. (1886).

[2] Schreyer *v.* Mills Co., 45 P. 719 (Oregon, 1896); Weatherford R. R. *v.* Granger, 34 S. W. 793 (Texas, 1894); Huron Co. *v.* Kittleson, 57 N. W. 234 (S. Da. 1894); Rogers *v.* Land Co., 134 N. Y. 197 (1892).

under a contract made prior to its formation, it would seem that on theory the only ground of recovery would be in quasi-contract. The point, however, has not so far arisen.

§ 3. *What constitutes corporate knowledge.*

It will be necessary in this connection to investigate briefly what is considered the knowledge of the corporation. In *Davis Wheel Co.* v. *Davis Wagon Co.*,[1] it was said: "The authorities do not agree whether a corporation is to be held cognizant of facts which have come to the knowledge of an officer or director unofficially; but the better opinion would seem to be that if the officer or director is an active agent of the corporation in the transaction affected by his knowledge, it is not material how or when he acquired his information."

Taking the opinion here expressed to be the better one, it is well settled that notice of facts to individual stockholders or corporators is not notice to the corporation[2] of those facts. The same rule pertains as to a director.[3] Notice to an agent, however, whose duty it is to disclose his knowledge is notice to the company.[4] The knowledge of the officers of a company is its knowledge.[5]

So, in *Rogers* v. *Land Co.*,[6] the corporation had been formed by joint holders of land under an agreement among themselves, that the company should serve a certain purpose, the owners becoming officers and directors. The Court, in enforcing the agreement, said: "The corporation was charged by the knowledge of its directors, the source of its title, and the consideration paid for the land, with notice of the proceedings of the bondholders which led to its existence, as well as their object in causing it to be organized."

[1] 20 Fed. Rep. 699 (1884).

[2] Housatonic Bank *v.* Martin, 1 Met. (Mass.) 294 (1840).

[3] Custer *v.* Tompkins Co. Bank, 27 P. S. 132; Weatherford R. R. Co. *v.* Granger, 24 S. W. 795 (Texas, 1894).

[4] Burt *v.* Batavia Paper Co., 86 Ill. 66 (1877).

[5] McDermot *v.* Harrison, 9 N. Y. Supp. 184 (1890); Bommer *v.* Spiral Hinge Co., 81 N. Y. 469 (1880).

[6] 134 N. Y. 197 (1892).

§ 4. *Where the promoter's contract would have been ultra vires or illegal if made by the corporation, the company not bound.*

It is also generally said that only acts within the scope of the corporate powers and such as are not against law or public policy can be adopted.[1] In view of the fact that the basis of the obligation created by this so-called adoption is, as we have seen, an implied contract, this statement must be taken to mean, not that the jury would be unjustified in finding that the corporation had intended to make an *ultra vires* or illegal contract, but that the effect of such intention was a nullity, and that the purpose of the company, however clearly expressed by words or actions, was inoperative to create a valid contractual relation. The same thought is apparent in the cases employing the doctrine of ratification, and was noticed under that head.[2] Again, wherever a formal action by the board of directors, or other corporate officers, is required by statute or the corporate charter, in order to bind the company if it were acting in the first instance, a like formality must have taken place before the company is bound.[3] The whole question belongs rather to the law of *ultra vires* acts of corporations than to that of contracts.

CHAPTER VIII.

WHERE THE PROMOTER'S CONTRACT PROVIDES FOR THE RENDERING OF SERVICES PARTLY BEFORE AND PARTLY AFTER INCORPORATION.

§ 1. *A contract implied in fact.*

The second class of cases to be discussed comprises those in which the employment or benefits rendered by the plaintiff, and on account of which he is suing, were so rendered partially before and partially after incorporation, in compliance

[1] Munson *v.* R. R., 103 N. Y. 58 (1886); McArthur *v.* Times Printing Co., 51 N. W. 216 (Minn. 1892); Schreyer *v.* Turner Mills Co., 43 P. 719 (Oregon, 1896); Burden *v.* Burden, 4 N. Y. Supp. 499 (1896).

[2] See ante, p. 46.

[3] McArthur *v.* Times Printing Co., 51 N. W. 216 (Minn. 1892); Schreyer *v.* Turner Mills Co., 43 P. 719 (Oregon, 1896).

with the terms of a contract made with the company's promoters; the company accepting that part rendered after incorporation with full knowledge of the terms of the contract.

As to the services rendered after organization, there are here, as in the former cases, all the elements of an implied contract. The question which arises, is as to whether there can be implied from the action of the company in accepting such services, a promise to pay not only for them but for those rendered before incorporation.

It would seem that since, by supposition, the corporation knew that the benefits which it accepted were rendered in compliance with the general terms of an arrangement under which former benefits had been conferred, it would not be a strained construction of its conduct to imply a promise on its part to pay for all. The only other question, therefore, would be as to whether, granting the promise, there was an adequate consideration to make it binding. And since the benefits rendered after incorporation would not have been conferred, except for the existence of the contract and the belief that compensation was to be made according to its terms, *i. e.*, for *all* the benefits rendered, there would seem to be a sufficient consideration moving to the corporation to support the implied promise to fulfil the promoter's engagement in all its particulars. In other words, the rendering of the services after incorporation is the consideration for the promise to pay for those formerly rendered.

In *McArthur* v. *Times Printing Co.*,[1] suit was brought for damages for breach of contract in discharging the plaintiff contrary to the terms of an agreement made by the promoters. Plaintiff had been employed before incorporation to solicit advertisements for the company, and after the charter was granted the company, knowing that the engagement had been for the term of a year, continued to make use of the plaintiff's services and to make him payments on account as required by the contract. The plaintiff was discharged without cause within the year.

[1] 51 N. W. 216 (Minn. 1892).

The Court held that the jury were justified in finding that the corporation had adopted the contract, explaining that by adoption was to be understood the making of a new contract of the date of the adoption, and the plaintiff was awarded damages for breach of contract.

Such a result could not be reached except upon the hypothesis that the implied contract created by the act of the company was of the same terms as that made by the promoters, and if so, included an undertaking to pay for services rendered before incorporation, as well as for those rendered afterwards, and to continue to employ the plaintiff during the term of one year. See also [1]

§ 2. *A limitation of the rule.*

In *Weatherford R. R.* v. *Granger*,[2] the action was brought upon account for services rendered before organization in procuring a bonus for the company, and also for services rendered subsequent thereto, as attorney. There was a judgment for the plaintiff for the whole amount. On appeal the Court decided that there could be no recovery for the services rendered prior to organization, though stating that "the evidence was sufficient to sustain a recovery by plaintiff for the value of his services rendered *after* the corporation was created." As the Court below had failed to find separately the reasonable worth of such services, the entire judgment was reversed.

Here there was no single contract regulating the terms upon which the plaintiff's services were rendered, and in fact there had been no agreement as to the compensation to be charged. A jury would not have been warranted in finding that because the company knowingly accepted the benefits rendered after incorporation it had thereby intended to promise payment for those rendered prior thereto. The case suggests the limitation, therefore, that in order to charge the corporation for benefits conferred before incorporation, by reason of

[1] Arapahoe Investment Co. *v.* Platt, 39 P. 584 (Colo. 1895); Grape Sugar Co. *v.* Small, 40 Md. 395 (1874).

[2] 24 S. W. 795 (Texas, 1894).

its acceptance of benefits rendered after incorporation, the services must have been given in respect of the same contract or employment; of which the company must have had knowledge.

CHAPTER IX.

When the Services have been Rendered before Incorporation.

§ 1. *Elements of a true contract absent.*

The third class of cases to be discussed comprises those in which the contract between the promoter and the one now suing the corporation has been fully executed by the latter before the company came into existence.

Under such circumstances the elements of a true contract are wanting. Even if the corporation makes use of and enjoys the fruits of the promoter's contract, (since it came into existence with these advantages already conferred upon it), it is impossible to say that, judged by the standards of reasonable men, its conduct in so doing must be intended to imply a promise to pay for them.

The moment the corporate body became instinct with life (by no voluntary act of its own), it was vested with the benefit of all the services rendered in its formation, with all the goods which had accrued to it in its inchoate condition. It is therefore impossible to make use of the fiction of the continuing offer, or to predicate an acceptance of an offer whose terms have been fulfilled.

Even if the corporation should expressly promise to pay, it would seem that the promise could not be enforced against it on the ground of lack of consideration, for it is a familiar principle of contract law that a past consideration is insufficient to create a binding obligation.[1] The only exception to the rule last stated occurs where a prior request has been made, after which, if services are rendered, a subsequent promise to pay will be enforced. But here we have no prior

[1] Eastwood *v.* Kenyon, 11 Ad. & El. 438; Anson, p. 102.

request, for unless the promoters can be treated as agents (a view long since discarded), they could have no more authority to make a request in behalf of the corporation than to bind it absolutely by contract. Such a power would impute privity between the promoters and the corporation, which does not seem to exist.

It may, nevertheless, be manifestly equitable in a large number of cases to charge a corporation for the money, time and labor expended in the necessary and reasonable measures preliminary to its organization, and this in spite of the fact that on the contract under which the work was done or the money expended, the promoters are primarily liable. It is equitable not only because the party contracting relied on the corporation for his compensation for the services rendered to it (and not upon the promoter who may have been but a man of straw), but also on account of the promoter himself who would be held personally liable if the corporation did not pay, and who has acted *bona fide* in its behalf and to its advantage.

§ 2. *The obligation, if any exists, is quasi-contractual.*

Under such circumstances we have not the elements of a true contract, but such an equitable claim against the corporation as the law is accustomed to enforce under the designation of a contract implied in law or a quasi-contract. This claim is based on the theory that, did not the corporation pay for the services rendered, it would be unjustly enriched at the expense of the plaintiff; and that the law will not permit such unjust enrichment, is an established doctrine.[1]

In speaking of the cases in which the doctrine is applied, Mr. Keener says:[2] "As the question to be determined is not the defendant's intention, but what in equity and good conscience the defendant ought to do, the liability while enforced in the action of assumpsit is plainly of a quasi-contractual and not contractual nature." The same writer says in a later

[1] Keener on Quasi-Contracts, p. 19.
[2] Quasi-Contracts, p. 20.

passage:[1] "Where the benefit for which the plaintiff seeks a recovery was conferred without the assent of the defendant there can of course be no contract, and unless the facts would establish a liability in tort, the plaintiff must proceed on the theory of quasi-contract."

If what has been said is true, the results which we may expect to find among the cases dealing with corporate liability for services rendered or benefits conferred *before* incorporation, can be summed up as follows:

1. No true contract can be implied against the company.

2. There can be no express contract without a new consideration.

3. There may be a contract implied in law if the facts of the particular case would warrant the Court in finding that there would otherwise be an unjust enrichment of the defendant at the expense of the plaintiff. . . .

4. Unless the Court takes the view that it is unjust to the stockholders and against good policy to imply a contract in such case, under which view no recovery is possible.

§ 3. *No contract implied in fact.*

First, then, as to whether there can be a contract implied in fact where the services have been rendered before incorporation. The case of *Rockford R. R. Co.* v. *Sage*[2] was an assumpsit against the company for money paid and surveying done during the organization of the road. The Court said: "We are disposed to deny the right of recovery for such services and expenses upon any *implied promise resulting from the facts*, although the case cited by appellee's counsel of *Low* v. *The R. R. Co.*[3] seems to sanction such a right of recovery." This decision has been expressly followed in the late Illinois cases.[4]

It is to be noted that *Low* v. *R. R. Co.*, "cited by appellee's

[1] Quasi-Contracts, p. 24.
[2] 65 Ill. 388 (1872).
[3] 45 N. H. 375 (1864).
[4] Western Screw Co. *v.* Cousley, 72 Ill. 531 (1874).

counsel," treated of a contract implied in law,[1] and is not in conflict with this opinion, in that respect, as was supposed by the Court. It did not decide that a true contract could be implied under such circumstances.[2]

In *R. R. Co.* v. *Ketchum*,[3] the appellee had rendered services in the formation of the road, and in acknowledgment thereof the company when formed had voted him a free pass. This they subsequently revoked, and he continued to ride in the company's cars, refusing to pay on the ground that the pass had been given in return for his services, and constituted an irrevocable contract. The determination of the question, whether such a contract had been made and whether there had been any consideration moving to the company on which to base it, was therefore necessary to the decision. Ellsworth, J., said: "We are aware that it is no uncommon practice for corporations to assume and pay these preliminary and antecedent charges after the company has been organized, but we do not see how the company, if it should object, could be compelled to pay them, and in some cases it would be most inequitable to require it. . . ." "It is soon enough for corporate bodies to enter into contracts encumbering their property when they are duly organized according to their charters, and have their chosen and impartial directors to conduct their business."

This case, while clearly deciding that no contract is created by implication from the circumstances, seems to go further and incline to the opinion that neither could there be a recovery on any grounds.

There are a number of cases which take this view, the reason of which will be discussed later,[4] but for the present it is only necessary to say that all of them support the proposition here contended for (*i. e.*, that there can be no contract implied in fact when it appears merely that a corporation has been benefitted by services rendered before complete organization), for

[1] See *infra*, p. 72.
[2] See *infra*, p. 73.
[3] 27 Conn. 170 (1858).
[4] *Infra*, p. 81.

they hold that such circumstances give rise to no legal obligation whatsoever.[1]

A contrary opinion, however, seems to have been entertained in some cases.

In *Paxton Cattle Co.* v. *Bank*,[2] the corporators having a preliminary organization, bought a ranch and gave a note therefor purporting to be a corporate obligation, and upon which suit is now brought. The Court said: "The company through its officers and manager has retained the possession of the property in Chase County, both real and personal, for which the said note was given. This, under the authority of the foregoing cases (*Low* v. *R. R. Co.* and *Bell's Gap* v. *Christy*),[3] is the turning point in the case, and I think the conclusion is inevitable, granting the entire want of power on the part of the officers and promoters of the corporation to act as such at the date of the note, that the retaining possession of the consideration by the corporation after its organization is a ratification of the contract with all of its terms and obligations."

The meaning of the Court is by no means clear in this decision, but it must be taken to intend one of two things. In refering to *Low* v. *R. R. Co.*, the Court had in mind a case in which it was said that "the contract is implied by law," and in saying that the retention of the benefit was the turning point, the Court may have meant that a quasi-contractual obligation was thereby created.

In saying, however, that the retention of the consideration "is a ratification of the contract," the Court would seem to infer that a jury would be justified in finding that it was the intention of the corporation to adopt or ratify the contract. In other words they base the obligation with which they charge the company upon intention, and not upon an implica-

[1] Weatherford R. R. Co. *v.* Granger, 24 S. W. 795 (Texas, 1894); Melhado *v.* Porto Alegre Co., L. R. 9 C. P. 503 (1874); Western Screw Co. *v.* Cousley, 72 Ill. 531 (1874); Rockford R. R. Co. *v.* Sage, 65 Ill. 388 (1872); Franklin Fire Ins. Co. *v.* Hart, 31 Md. 60 (1869); Marchand *v.* Loan & Pledge Assn., 26 La. Ann. 389 (1874); Abbott *v.* Hapgood, 150 Mass. 248 (1889).

[2] 21 Neb. 621 (1887).

[3] *Infra*, § 6.

tion of law. If such was the thought of the Court, it is respectfully submitted that it is not in conformity with the authorities already considered, nor does it rest on sound principle.[1]

§ 4. *An express promise not enforcable without a new consideration.*

The second conclusion which seemed probable, according to the discussion in the earlier part of this chapter, was that even if there should be an express promise on the part of the corporation to pay for the services rendered before its incorporation, such promise could not be enforced except on the basis of a new consideration; the benefit being past.

In *Melhado* v. *Porto Alegre R. R. Co.*,[2] the declaration counted for a breach of contract, and set forth that plaintiff had at the instance of the promoters of the company expended £2000 in necessary preliminary expenses. That the articles of association provided for the payment of all such expenses (if the directors should subsequently approve of them), and that the directors of the company had expressly ratified his expenditures.

Coleridge, J., refused to allow a recovery in spite of the formal action of the board of directors after the company was formed; thus denying that a binding contract had been created.

In *Empress Engineering Co.*[3] the board of directors after incorporation passed a resolution "that the agreement of purchase be ratified." Jessel, M. R., however, refused to hold the corporation bound by the action of the board.[4]

The contrary conclusion, however, has been suggested in some Illinois cases, though the point was not squarely decided. It was said in *Rockford R. R. Co.* v. *Sage*:[5] "For services

[1] See, however, to the same effect, Buffington *v.* Bardon, 50 N. W. 776 (Wisc. 1891).

[2] L. R. 9 C. P. 503 (1874).

[3] 16 Ch. Div. 125. (1880).

[4] See also Abbott *v.* Hapgood, 150 Mass. 248 (1889).

[5] 65 Ill. 388 (1872).

and expenses before the organization of the company which subsequently the company accepts and receives the benefit of and promises to pay for, we will not say a party might not recover in virtue of such express promise;" but none such appeared in the case.

Following this suggestion, the dictum was repeated in *Western Screw Co.* v. *Cousley*,[1] where it was said: "This Court has decided that a corporation, after its organization, is not liable for the payment of debts contracted previously thereto, at least, without an express promise to pay them after acceptance and receipt of the benefit of that for which they were incurred."

As before said, the point was not necessary to either of these decisions, nor does it seem to have been duly considered or the objections thereto brought forward, so that the suggestion may safely be ignored, and as far as these cases are concerned, the rule stands as stated, *i. e.*, that even an express promise to pay for services rendered before incorporation does not bind the company without a new consideration.

Rather more difficulty, however, is occasioned by the case of *Stanton* v. *N. Y. & Eastern R. R. Co.*[2] The case was this: There having been a preliminary organization of the company, the plaintiff had entered into a contract with the *pro tempore* directors, agreeing to purchase the rights of way necessary for the road, according to certain stipulations. He did so. After organization the company passed a resolution that "the foregoing contract is ratified and declared to be a binding contract upon the parties." But the road failed and could not pay. The receiver appointed disallows the claim, and the plaintiff appeals from his report, which the lower Court had accepted. The Court said: "The corporation, by its ratification of the contract previously made by its promoters, became liable for everything that had been done pursuant to it. . . . The directors acted with full knowledge of all the facts and with such knowledge they ratified the contract. . . . Ratification relates back to the execution of the contract and renders it

[1] 72 Ill. 531 (1874).
[2] 59 Conn. 272 (1890).

obligatory from the outset. By the nature of the act, the party ratifying becomes a party to the contract and is on the one hand entitled to all its benefits and on the other is bound by its terms." The lower Court was reversed and the Court indicated that the plaintiff was entitled to recover for his time, money and labor expended; and damages for breach of the contract.

This decision is to be explained on the ground that the Court was clearly of opinion that in such cases the technical doctrine of ratification is applicable. However much the soundness of this view may be questioned,[1] it may be taken as settled that, wherever this doctrine of ratification is employed, no new consideration is needed to make the promise binding, for no new contract is made. As was said by Sharswood, J., in *Negley* v. *Lindsay*,[2] in reference to the doctrine of ratification: "The party confirming becomes a party to the contract, he that was not bound becomes bound by it; he accepts the consideration of the contract as a sufficient consideration for adopting it and usually this is quite enough to support the ratification."

In all those cases, therefore, where the technical doctrine of ratification is made use of or in which the Court says that there may be an actual adoption of the original contract, there being no new contract made, the corporation may be bound either expressly or impliedly without a new consideration.

But for this reason the cases are not authority against the general proposition that the company may not bind itself for benefits antecedent to incorporation, without a new consideration.

§ 5. *The doctrine of quasi-contract.*

We now come to consider the cases in which it is held that the law will impose an obligation to pay, where the corporation has been benefited unjustly at the expense of the plaintiff.

As has been said, the basis of this quasi-contractual obligation lies in the *injustice* of the defendant's enrichment at the

[1] See ante, p. 43 *et seq.*

[2] 67 Pa. 218.

expense of the plaintiff. As to what constitutes "injustice," no rules of law can be laid down. Its presence or absence in any case must be determined by the circumstances of the particular transaction, viewed with reference to that standard of fairness and "good conscience" existing in the mind of the average reasonable man.

The position in which a corporation finds itself when confronted with a claim for services rendered before incorporation has this peculiarity. Not only were the services rendered without its request, but it never had an opportunity to refuse to accept them, and what is more it cannot return them. Under such circumstances, if the law is to impose an obligation upon the corporation to compensate the plaintiff, the most rudimentary conceptions of justice would dictate that the services or benefits, for which the claim is brought, must have been necessary to the formation of the company, and reasonable in view of the purposes for which it was to be created. Were either of these elements absent, the company would be compelled to pay for that for which it neither sought nor was in need.

Again, the services must have been of value to the corporation; for no matter how strenuously the plaintiff has labored or how much time and money he has expended, (if he has not succeeded in giving to the corporation that of which it stood in need), he has no equity to require payment therefor, since it is to be remembered that he has acted either at his own instance or at the instance of those who had no authority to bind the company.

It would also appeal to the common sense of justice that where the plaintiff has not contracted in reliance on the corporate credit, but depending upon the promise of the promoter, and he has received all that he contracted for, viz, a right of action against the said promoter, he should not be allowed to have more than his bargain, by holding the company liable.

In a general way, these are some of the thoughts which in any given case would effect the question of the justice or injustice of allowing a recovery against a corporation.[1]

[1] Keener's Quasi-Contracts, Chaps. VI. and VII.

§ 6. *The doctrine as applied in the cases.*

Bearing these thoughts in mind, let us consider how far the doctrine of "unjust enrichment" has been recognized, by an examination of the cases.

In re Empress Engineering Co.[1] was a suit by an attorney for £63 for services rendered in procuring the charter of the defendant corporation. The articles of association provided for the payment of that sum, and the board of directors had expressly ratified the agreement after incorporation. The plaintiff brings his suit as upon an express promise.

Jessel, M. R., in denying a recovery, said: "There is another ground suggested, namely, that as the company has had the benefit of the registration they ought to pay for it. But the answer to that is, that that was not the claim brought forward. The claim brought forward was for an agreed sum of £63, and any order we may make will not prejudice that claim, which is merely for an amount due for services, the benefit of which has been taken by the company."

In *Low* v. *R. R. Co.*,[2] Bellows, J., said: "We are inclined to think, however, that it is no violation of settled principles to hold that a suit at law may be maintained to enforce the obligation to pay for services rendered in the manner described (under a contract with a promoter before incorporation), and of which the corporation after its organization has taken the benefit. If it were true that, at the time the services were rendered, the corporation had no capacity to make a contract, which is by no means clear after the charter has been accepted, still if the service were rendered for the corporation upon the promise of the corporators that they should be paid for by it when its organization was perfected, and after that the corporation had adopted the contract and received the benefit, we think that upon the maxim that a subsequent ratification is equivalent to a prior request, it may well be held that a promise to pay will be implied. Upon this principle a person may sue on a contract made in his name by one assuming to have authority

[1] L. R. 16 Ch. Div. 125 (1880).
[2] 45 N. H. 375 (1864).

but having none in fact. . . . *But the promise is implied by law* from the fact that the party, when it had capacity to contract, has taken its benefits and, therefore, must be deemed to have taken its burdens at the same time, and he is estopped to controvert it either by showing a want of capacity to make a contract or that none in fact was made." . . . "Indeed, it would be immaterial whether such services were rendered by a corporator or another, because the subsequent ratification is equivalent to an antecedent request; but we think that without such ratification, either express or implied, from taking the benefits of such services, the law would raise no such promise to pay, from the mere fact that the plaintiff was requested to render them by one of the original corporators or associates."

This amounts to a statement that, unless the corporation received benefit from the services, it would not be unjustly enriched at the expense of the plaintiff, and therefore no recovery could be had on that ground; and when the Court says that since the corporation would not be bound by the act of one of the promoters only, unless benefit had accrued to the corporation, it intimates that it would be bound in spite of the fact that *no* benefit accrued, if all the corporators had assumed to bind it.

That these two possibilities were before the mind of the court is apparent from the statement that it is not at all clear that the corporation is not sufficiently *in esse* to be bound by the acts of its officers after it has received a charter, though no organization has taken place. The thought is, first, that the corporation is *in esse* and may be bound; and, second, apart from that "if the services were rendered . . . and the corporation . . . received the benefit . . . a promise to pay will be implied."

In this case all the elements of a quasi-contract or a contract implied in law are present. Reasonable and necessary services had been rendered to the corporation, at the instigation of the promoters, of which the company had had the benefit, and for which they refused to pay. There was an unjust enrichment at the expense of the plaintiff. Indeed, the express language of the Court is to the effect that the contract so called is

implied by law. No doubt whatever could exist, were it not that the doctrine of ratification is dragged in and the statement made that the promise will be implied "upon the maxim that a subsequent ratification is equivalent to a prior request," and that "upon this principle a person may sue on a contract made in his name by one assuming to have authority but having none in fact." In other words, the Court makes use of the technical doctrine of ratification in order to charge the company, and must therefore have been of opinion that the intention of the corporation to be bound was necessary in order to create a contract implied in law. Now it is respectfully submitted not only that the doctrines of agency and of ratification have no connection whatever with the quasi-contractual obligation which the Court in fact imposed, but that the intention of the corporation to be bound is also entirely unnecessary in order that such obligation should be created. As said by Mr. Keener,[1] in relation to the term "contract implied in law," "It is a term used to cover a class of obligations where the law, though the defendant did not intend to assume an obligation, imposes an obligation upon him, notwithstanding the absence of intention on his part, and in many cases in spite of his actual dissent."

It would seem, then, that while the Court in this case recognized that the obligation to be enforced against the defendant was quasi-contractual rather than contractual, it did not have clearly in mind the elements of such quasi-contractual obligation, and considered that there must be something in the nature of a ratification or an expression of willingness to be bound before the company could be charged. They also intimate that the mere passive retention of the benefits would be a sufficient circumstance from which a so-called ratification could be implied.

Now it is to be noted that if the facts were sufficient to give rise to an implication that the corporation had intended to pay, then a true contract would have existed between the parties, and it is believed that the law will never imply a contract

[1] Quasi-Contracts, p. 5.

where one already exists in fact,[1] for its primary aim is to give effect to the intention of the parties.

Again, if the obligation were dependent upon an implication from the facts, it is submitted that the Court erred in considering that, from a mere passive retention of the benefits, it could be inferred, as a matter of fact, that the corporation had promised to pay for them. The benefits referred to were services rendered in the formation of the company and the procuring of the charter. They were intangible and impossible of restitution. The corporation could not have refused to accept them since it came into being involuntarily, nor could it have refunded them, nor failed to use them without ceasing to exist. Under such circumstances it is submitted that a jury would have been utterly unjustified in finding any expression of intention on the part of the corporation. In all such cases, if the facts give rise to an equitable claim against the company, the remedy must be in quasi-contract, and if the Court shall determine in any case that there has been an unjust enrichment at the expense of the plaintiff, it is unnecessary for it to go further and attempt, as here, to find some expression of willingness to be bound.

This being the primary cause of confusion in the case, it is also to be remembered that the Court intimates, as an entirely distinct proposition, that a charter having been granted, the company was *in esse* and could be bound by the action of a majority of the corporators, as it could be by its regularly constituted officers.

The Pennsylvania case of *Bell's Gap R. R. Co.* v. *Christy*[2] was decided on the authority of this case. That was an assumpsit for services rendered and money expended in procuring the charter of the defendant company. Those present at a meeting before the charter, authorized plaintiff to do the work, and promised that he should be paid.

Paxson, C. J., said: "This lacks all the elements of a contract express or implied." In *Low* v. *R. R. Co.*, it was held

[1] Keener, p. 328.
[2] 79 Pa. 54 (1875).

that "where, after the charter and before the organization of a corporation, services are rendered which are necessary to complete that organization, and after it has been perfected the corporation elects to take the benefit of such services, knowing that they were rendered with the understanding that compensation was to be made, it will be held liable to pay for the services upon the ground that it must take the burden with the benefit; but that '*no promise to pay would be implied from the fact that such services were rendered at the request of any number of the corporators, less than a majority.*'"

"It may very well be that where a number of persons not incorporated are yet informally associated together in the pursuit of a common object, and with the intent to procure a charter, in the futherance of their design, they may authorize certain acts to be done by one or more of their number, with an understanding that compensation shall be made therefor by the company when fully formed. And if such acts are necessary to the organization and its objects, and are subsequently accepted by the company and the benefits thereof enjoyed by them, they must take such benefits *cum onere* and make compensation therefor. But the projectors or promoters of the enterprise within the meaning of the rule referred to, evidently must be a majority, at least, of such persons. Such minority can have no more authority to bind the association or corporation in its incipient or inchoate condition than they would have to bind it if fully organized." . . . "In the absence of any such authority *and* of any satisfactory proof that the result of the plaintiff's labor and expenditures was accepted and enjoyed by the corporation," . . . the defendant is not liable.

As we have seen the Court, in *Low* v. *R. R. Co.*, suggested two theories, on either of which that case might have been rested; the first, that the charter having been granted the corporation was *in esse* and could be bound by the acts of the corporators (in which case of course a majority must act); the second, that the company might become bound on a contract implied in law.

Now, the Court while purporting to quote from *Low* v. *R.*

R. Co., uses language not to be found therein,[1] but which appears only in the syllabus of that case, and the statement as transcribed by the reporter is without any regard to its connection in the opinion. By adopting the words of the syllabus in *Low* v. *R. R. Co.*, the Court confuses the two grounds of action referred to, and while treating of the obligation as quasi-contractual, comes to the anomalous conclusion that not only must the corporation have been unjustly enriched, but the services must have been induced by a majority of the corporators before a recovery can be had against it. That the obligation is conceived of by the Court as resting in quasi-contract rather than contract is apparent from the following language: "And if such acts are necessary to the organization and its objects, and are subsequently accepted by the company and the benefits thereof enjoyed by them, they must take such benefits *cum onere* and make compensation therefor." Nothing is said about intention, and the Court wisely avoids the confusion of the suggested "ratification" of the Low case, and rests the duty of the corporation to pay, on the firm ground of the unjust enrichment which would occur in the event of its being permitted to refuse to compensate the plaintiff. Unfortunately, however, through the misinterpretation referred to, the conclusion reached, is undoubtedly, that the elements of a quasi-contract being present, the law will not enforce the obligation unless in addition the services were rendered at the request of a majority of the corporators. There is neither authority nor apparent reason to support such a rule.

This mistake led to confusion in the later Pennsylvania case of *Tift* v. *Bank*.[2] That was an assumpsit for services rendered after preliminary, but before final organization, in procuring subscriptions to stock at the request of a promoter. After organization was completed, Tift applied to the promoter (who was now president of the bank) for payment. The president promised that he should be paid, and subsequently laid the

[1] See portion of opinion in italics.

[2] 141 Pa. 550 (1891).

matter before the directors who made no objection but took no action on the matter. This evidence was refused admission as immaterial and judgment rendered for the defendant.

On appeal the Court said: "It is true it was said in *Bell's Gap R. R. Co.* v. *Christy*,[1] that where a number of persons not incorporated but associated for a common object, intending to procure a charter, authorized acts to be done in furtherance of their object by one of their number with the understanding that he should be compensated; if such acts were necessary to the organization and its objects, and are accepted by the corporation and the benefits enjoyed, they must be taken *cum onere* and compensated for. But it was also said that the promoters of the enterprise must be a majority. In the case in hand, the promise was made by a single promoter and there is no evidence of a subsequent ratification by the corporation." Judgment for defendant affirmed.

It has already been suggested that it would be a possible view to take of these cases, that in spite of the possibility that a corporation might be unjustly enriched at the expense of one who has rendered it material services before incorporation, a recovery should not be allowed in any event on the ground that the rights of shareholders who bought stock without knowledge of the services, would in some cases be impaired. If recovery is to be permitted at all, however, it would seem that in all justice it should be allowed in a case such as the one under discussion. No question was raised by the defendant as to the value, the reasonableness, or necessity of the services rendered. The plaintiff acted under a contract made on behalf of the company by the promoter chiefly interested in the scheme, and with the expectation that the company would pay him when it came into existence. The plaintiff has been injured and the defendant benefitted. The elements of the quasi-contractual obligation are all present; and yet, as we have seen, the Court denies a recovery on the ground that a prerequisite is still lacking in that all of the promoters did not join in requesting the services. The reason given for the

[1] 79 Pa. 54 (1875.)

result reached is, it is submitted, inadequate and based as has been shown on a misinterpretation of authority.

In a recent New York case,[1] the quasi-contractual nature of the remedy seems to be recognized though the opinion is too short to be very satisfactory.

The action was brought against the company for work done before incorporation at the request of a promoter and which, as the declaration alleged, went to the benefit of the company. The Court contented itself with saying: "The work was evidently done in contemplation of the corporate formation and it went to its benefit. Mr. Hazard, who ordered the work, seems to think he should not pay for it because the corporation got the benefit of it, and the corporation thinks it ought not to pay for the work because Hazard ordered it. This may sound well to all concerned except the plaintiffs who are entitled to their earnings." Judgment was rendered for the plaintiff. See also[2]

§ 7. *The reasons urged against permitting a recovery in quasi-contract.*

It has been frequently indicated throughout the foregoing discussion that a view prevails in certain jurisdictions that, as regards these services rendered antecedent to the formation of the company, the circumstances can give rise to no true contract based on the intention of the parties, nor will the law imply an obligation on the part of the company to compensate those who rendered them. These cases proceed upon the ground that it is unjust to stockholders to subject their property to the payment of claims in whose creation they took no part and whose legitimacy, therefore, they had no voice in determining.

The objection does not appear to be altogether well founded in this respect. Since the obligation rests on the doctrine of unjust enrichment, it only arises where the corporation (and therefore the stockholders) has received an actual benefit, for

[1] Grier *v.* Hazard & Co., 13 N. Y. Supp. 583 (1891).
[2] Little Rock, Etc., R. R. Co. *v.* Perry, 37 Ark. 164 (1881).

which it is unjust that it should refuse to compensate the plaintiff. We have seen that, in the cases in which the doctrine has been employed, it has been uniformly held that the company was not *unjustly* enriched unless the benefits received were reasonable and necessary to the formation of the company. Now, under this rule, it would seem that it is no hardship to charge the stockholders for what was necessary to the corporate existence.

Another safeguard against undue recoveries against a corporation lies in the rule that the plaintiff must have relied upon the credit of the defendant; for if he acted upon some other consideration the benefit accruing to the corporation is purely incidental, and it is no injustice to refuse compensation therefor.[1]

Again, the plaintiff is bound to take himself out of "the well established rule that no one has a right to force himself upon another as his creditor."[2] So, in any case in which the Court should be satisfied that the plaintiff had acted at his own instigation for the purpose of subsequently charging the company, it would seem that there could be no recovery. He must show that the services were rendered *bona fide* at the request of those interested in the formation of the corporation.[3] And finally a recovery on the quasi-contractual obligation does not follow the terms of the original agreement between the plaintiff and the promoter, but is measured by the amount by which the defendant has been unjustly enriched.[4]

Under these circumstances it seems highly improbable that the rights of stockholders would be infringed in any considerable number of instances, and it is submitted that this would be a lesser evil than to refuse compensation, in any event, to those who have *bona fide* expended time, labor and money in the creation of a corporation.

[1] Wilbur *v.* N. Y. Co., 12 N. Y. Supp. 456 (1891); Little Rock R. R. Co. *v.* Perry, 37 Ark. 164 (1881); Weatherford *v.* Granger, 24 S. W. 795 (Texas, 1894); Keener, pp. 350, 361.

[2] Keener, p. 341.

[3] Hall *v.* Vermont, Etc., R. R. Co., 28 Vt. 401 (1856); Low *v.* R. R. Co., 45 N. H. 370 (1864).

[4] Keener, Chap. VII.

§ 8. *The cases denying such a recovery.*

A considerable number of cases, however, take a contrary view. The leading case in America is *R. R. Co.* v. *Ketchum*,[1] which has already been considered at length. It will be recalled that the Court there used the following language in regard to allowing a recovery for expenses antecedent to incorporation. "This would be a breach of faith towards honest and unsuspecting stockholders who pay the charter price for their stock and expect to take it clear of all incumbrances. The getters-up of projects to be carried by such means may well be supposed, as is generally the fact, to be influenced by a view to their own special benefits, for certainly they do not act in behalf of the corporation itself. . . . It is soon enough for corporate bodies to enter into contracts incumbering their property when they are duly organized according to their charters and have their chosen and impartial directors to conduct their business."

Though the language of the Court is sufficiently broad to include all antecedent expenses, it was not necessary to the decision of the case, for the evidence was not clear that the services had been rendered with the primary intention of benefitting the intended corporation. In such a case the benefit is merely incidental, and falls within the rule that the law will not imply a promise to pay for incidental benefits conferred by one acting primarily upon some other consideration.

The same thought appears in *Rockford R. R. Co.* v. *Sage*,[2] where the Court says, "A right of recovery against a corporation for anything done before it had a proper existence does not appear to rest on any very satisfactory principle. It appears more reasonable to hold any services performed or expenses incurred prior to organization to have been gratuitous, in view of the general good or private benefit expected to result from the object of the corporation," and the decision is rested on the case above cited.

[1] 27 Conn. 170 (1858).
[2] 65 Ill. 388 (1872).

The English authority on the subject is *Melhado* v. *Porto Allegre Co.*[1] The plaintiff declared for breach of contract in the sum of £2000 expended by him in necessary preliminary steps in the formation of the company. The articles of association directed the company to pay the same.

Coleridge, C. J., after explaining that the doctrine of ratification was inapplicable, said: "Then it was suggested that, by taking advantage of their work and expenditures and coming into existence through them, the company gave rise to an implied contract to remunerate them. It seems to me that the defendants' counsel gave the right answer to this suggestion when he said that, if that were so, promoters might in all cases sue the company for expenses of promotion. I apprehend that all the decisions on this subject show that they cannot do so."

It has been attempted to be shown that the result feared by the learned judge, is not one to be dreaded from an application of the doctrine of quasi-contract to these cases. The law does not imply the promise *eo instanti* a plaintiff shows that he has conferred a benefit upon the defendant company, but he must first show that the company has been *unjustly* enriched at his expense. It is only when there is a real equity against the company that the obligation can be enforced, and in such a case the reasoning of the Court would seem inadequate.

One of the latest of the American decisions upon this point, and a case in which the whole subject of corporate liability on account of the acts of promoters is carefully discussed, is *Weatherford, M. W. & M. R. R. Co.* v. *Granger*,[2] decided by the Supreme Court of Texas in 1894.

A preliminary organization of the railroad company having taken place, the then officers promised that if a bonus should be raised by subscription the road should run between certain towns. One Anderson, the chief promoter of the scheme, was commissioned by the members of the organization to raise the bonus, and for his services in so doing he was promised $1000.

[1] L. R. 9 C. P. 503 (1874).
[2] 24 S. W. 795.

Anderson, on his own authority, promised the plaintiff that if he would assist in procuring subscriptions to the bonus, the company would pay him. The bonus was raised, through the joint efforts of the plaintiff and Anderson, and the company was formed. The plaintiff now sues the company for recompense, for his services which the company had refused on the ground that its only contract was with Anderson. The plaintiff had also rendered services as attorney.

Gaines, J., held: "Now, when it is said that when a corporation accepts the benefit of a contract made by its promoters, it takes it *cum onere;* it is important to understand distinctly what is meant. There is, so far as this matter is concerned, a radical difference between a promise made on behalf of the future corporation in the contract itself, the benefits of which the corporation has accepted, and the promise in a previous contract to pay for services in procuring the latter to be made. This is well illustrated by the facts of the present case. Here a proposition was made on behalf of the company by its promoters, that if a bonus should be subscribed and paid to it, it would build its road between certain points and would carry coal at a certain stipulated rate. By accepting the bonus the company became bound to fulfil the stipulations of the contract. That was the burden which it took with the benefit of the agreement. But it also appears that one of the promoters promised the plaintiff that if he would assist in procuring subscribers to the bonus, the company would pay him for his services. This was no part of the contract, the benefits of which were taken by the defendant. The benefits of a contract are the advantages which result to either party from a performance by the other, and in like manner its burdens are such as its terms impose. A more accurate manner of stating the nature of the plaintiff's demand is, to say, that the defendant has accepted the benefit of the plaintiff's services and should pay for them. It is true in one sense that the company has had the benefit of plaintiff's services, and it is equally true that it would have had the benefit if the services had been rendered under an employment by the subscribers to the bonus; and yet in the latter case it could not be claimed

that the company would be liable for such services unless payment for them by the company were made one of the terms of the contract between the company and the subscribers. *In re Rotherham*, in the opinion of one of the justices, this language is used: 'It is said that Mr. Peace has an equity against the company because the company had the benefit of his labor. What does that mean? If I order a coat and receive it, I get the benefit of the labor of the cloth manufacturer, but does any one dream that I am under any liability to him? It is a mere fallacy to say that because a person gets the benefit of work done by somebody else he is liable to pay the person who did the work.' There is more doubt as to the plaintiff's right to recover for his legal services in advising as to the articles of incorporation and in correcting and preparing this paper. Such services are usually necessary, and it would seem that the corporation should pay for them. Such payment is frequently provided for in the act of incorporation or in the articles when the incorporation is effected under a general law. When such is the case, persons who take stock in the company are chargeable with notice that a liability for this purpose has already been created and it is proper for the corporation to discharge it. But in the absence of such provision in the statute or in the articles, it may be unjust to shareholders to charge the corporation with liabilities of which they had no actual knowledge at the time they accepted the shares. We, therefore, hold with some hesitation that claims for the necessary expenses of the organization under our statute should not be excepted from the general rule applicable to contracts made before the corporation has come into legal existence." See, also, to the same effect.[1]

The opinion of the learned judge is divided into two parts. In the first, he treats of the plaintiff's services in raising the bonus; in the second, of the services rendered as attorney. As to both classes, the conclusion reached is that there can be no recovery, but the results are based upon different grounds.

[1] Western Screw Co. *v.* Cousley, 72 Ill. 531 (1874); Marchand *v.* Loan & Pledge Assn., 26 La. Ann. 189 (1874); Franklin Fire Ins. Co. *v.* Hart, 31 Md. 60 (1869).

1. As to the first the Court says: "A more accurate manner of stating the nature of the plaintiff's demand is to say that the defendant has accepted the benefit of the plaintiff's services and should pay for them. It is true, in one sense, that the company has had the benefit of plaintiff's services and it is equally true that it would have had the benefit if the services had been rendered under an employment by the subscribers to the bonus." A clearer exposition of the nature of the quasi-contractual obligation could not be had. The Court acknowledges that the company has received a benefit at the hands of the plaintiff, but denies a recovery. Why? Is it not because there has been no unjust enrichment of the defendant? The services were, indeed, rendered at the instance of a promoter, and with the expectation that they were to be paid for by the corporation. But as far as the corporation is concerned, it has already paid for them under its contract with Anderson. In view of such payment to Anderson, the plaintiff's services were not necessary and the corporation is not in "equity and good conscience" bound to remunerate the plaintiff. There has been no "unjust" enrichment, and the Court is clearly right in refusing a recovery.

The same reason underlies those cases in which it is held that, if an owner of property incurs debts in improving it and then conveys to a corporation which he is instrumental in organizing, the company is not liable for the debts so incurred. The plaintiff urges that his money has gone to the benefit of the corporation and the law should create an obligation to see him paid; but the short answer is that the law is not called upon to make the company disgorge, for it has not been unjustly enriched.[1]

2. As to the plaintiff's labors as attorney, though the elements of the quasi-contractual obligation are present, a recovery is refused on the distinct ground that otherwise the rights of shareholders would be infringed.

In so deciding, the Court undoubtedly followed eminent

[1] Ruby Chief Mining Co. *v.* Gurley, 29 P. 668 (Colo. 1892); Little Rock R. R. Co. *v.* Perry, 37 Ark. 164 (1881); Paxton *v.* Bacon Mill Co., 2 Nev. 257 (1866).

authority, though, as has been suggested, the view might, perhaps, be entertained that since the shareholders are the real parties in interest, and since no recovery can be had, save where the corporation (and, therefore the shareholders themselves) has been unduly benefitted, it is no hardship upon the latter to allow the recovery.

CHAPTER X.

CONCLUSION.

It will be sufficient to say, in conclusion, that while there has been a very considerable difference of opinion among the Courts as to the grounds upon which a corporation is liable for benefits received under a promoter's contract *after* incorporation,[1] that this difference of theory has not led to any great divergence in the conclusions arrived at in the cases; for whatever the theory, the prerequisites to a recovery have been essentially the same in all Courts. The discussion given this question, therefore, must be justified rather as being in the interests of an exact use of legal terminology than as touching fundamental principles.

As regards the subject latterly considered, however, *i. e.*, as to the liability of a corporation for services rendered *before* incorporation, it has been seen that the decisions are squarely in conflict. Those denying a recovery have upon their side, perhaps, the weight of authority; while those permitting it have not applied uniformly and consistently[2] the principles of quasi-contract upon which it is contended such a recovery is based. It may be fairly said that both sides generally admit that if there can be a recovery under any circumstances, the foundation thereof must lie not in contract but in an obligation imposed by the law.

The thought of the writer has been that, in many instances, it would be but just and right that the law should create a

[1] See Part II.

[2] See Low *v.* R. R. Co., 45 N. H. 370 (1864); Bell's Gap *v.* Christy, 79 Pa. 54 (1875).

liability on the part of a corporation to pay for expenses preliminary to its organization; that the conflict of authority has, perhaps, arisen from a failure on the part of some of the courts to recognize the grounds upon which such an obligation rests; and I have, therefore, made free use of the thoughts contained in Mr. Keener's work on Quasi-Contracts, wherein the bases of this obligation are so ably considered.

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